TRANSCRIPT OF RECORD

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1940

No. 188

THE UNITED STATES, PETITIONER

vs.

COWDEN MANUFACTURING COMPANY

ON WRIT OF CERTIORARI TO THE COURT OF CLAIMS

PETITION FOR CERTIORARI FILED JUNE 27, 1940
CERTIORARI GRANTED OCTOBER 14, 1940

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1

In the Court of Claims

No. 44307

COWDEN MANUFACTURING COMPANY, PLAINTIFF

v.

UNITED STATES OF AMERICA, DEFENDANT

I. *Petition*

Filed Dec. 1, 1938

To the Honorable, the Chief Justice and the Judges of the Court of Claims;

I

The plaintiff is, and at all times hereinafter mentioned was, a corporation duly organized and existing under the laws of the State of Missouri, with its principal offices and place of business at 412 West 8th Street, Kansas City, Missouri, and engaged in the business of manufacturing garments, particularly service suits, overalls, playsuits, and pants for sale to various buyers, including the United States of America.

2

II

The plaintiff, in accordance with the general practice of public bidding required by law and followed by the various Departments of the United States Government, particularly the War Department, submitted its bid and obtained the award of Contract Number W669–2M4800 (O. I. 2538), dated June 24, 1933, and approved July 5, 1933, for shipment of 23,496 suits, mechanics type B–1 @ $1.90 or an aggregate price of $44,642.40, to supply the Quartermaster Corps, at Philadelphia, Pennsylvania, between June 24, 1933, and October 22, 1933. That pursuant to a change order dated July 5, 1933, approved August 8, 1933, under and by virtue of the provisions of Article 7 of said contract, the same was increased upon written order from the contracting officer of the War Department and the plaintiff was required to and did supply 11,724 additional suits, mechanics type B–1 @ $1.90 or an aggregate price of $22,275.60, making the total number of suits, mechanics type B–1, 35,220 @ $1.90, or an aggregate of $66,918.00 furnished under the said contract.

The plaintiff states that in accordance with said contract and all extension agreements made thereunder with the War Depart-

III

ment, the plaintiff agreed to sell and deliver to the defendant, the defendant agreed to accept delivery and did in fact accept delivery of the aforementioned mechanics suits, all of which is related more specifically as follows: The plaintiff shipped September 16, 1933, 12,480 mechanics suits for which it received payment that day the sum of $23,712.00 by check #52224,
3 shipped September 29, 1933, 6,522 mechanics suits for which it received payment on that day the sum of $12,391.80 by check #53474, shipped October 13, 1933, 4,900 mechanics suits for which it received payment on that day the sum of $9,310.00 by check #54707, and shipped 11,318 mechanics suits on November 10, 1933, for which it received payment of the sum of $21,504.20, making a grand total of 35,220 mechanics suits shipped to and a total payment of $66,918.00 by the War Department of the United States.

IV

Among other things plaintiff and defendant agreed that the prices set forth in the contract included any Federal Tax imposed by Congress prior to the submission of the plaintiff's bid and that said prices were to be increased or decreased accordingly, in the event that Congress should change said taxes subsequent to the opening of said bid, the exact provision of Article I being as follows:

"Prices set forth herein include any Federal Tax heretofore imposed by the Congress which is applicable to the material purchased under this contract. If any sales tax, processing tax, adjustment charge, or other taxes or charges are imposed or charged by the Congress after the date set for the opening of the bid upon which this contract is based and made applicable directly upon the production, manufacture or sale of the supplies covered by this contract and are paid by the contractor on the articles or supplies herein contracted for, then the prices named in this contract will be increased or decreased accordingly and any amount due the contractor as a result of such change will be charged to the government and entered on vouchers (or invoices) as separate items."

V

4 The plaintiff states that immediately upon execution of said contract with the War Department, it entered into agreements with certain subcontractors for the purchase of mate-

rials with which to manufacture the mechanics suits sold thereunder. That on the 23rd day of July, 1933, the plaintiff purchased from McCampbell and Company, 320 Broadway, New York, selling agents for Graniteville Manufacturing Company of Graniteville, South Carolina, 150,000 yards, 28 inch aviation corps material, olive drab, shrunk, @ 21¢, with the privilege of increasing the option 50%. That thereafter and on the 30th day of July, 1933, the plaintiff exercised its option agreement and did purchase an additional amount of the aviation corps material, aforesaid, at the contract price of 21¢ per yard.

That said goods, aggregating 213,127¾ yards were furnished by the said subcontractor and shipped to the plaintiff at stated intervals. Moreover, the plaintiff purchased 885⅔ units of thread from the American Thread Company and 33,897 cotton labels from the Artistic Weaving Company, all of which materials were furnished by said subcontractors to the plaintiff to be used in the manufacture of mechanics suits to fulfill the aforesaid contract with the War Department.

VI

That on May 12, 1933, the Congress of the United States enacted the Agricultural Adjustment Act by virtue of which, there was imposed upon the said subcontractors, subsequent to the date of the opening of the bid of the contract between the plaintiff and the defendant, certain processing taxes which said subcontractors were compelled to pay to the United States as follows:

McCampbell and Company, processing tax on 213,127¾ yards of aviation corps material, $4,425.54;

American Thread Company, processing tax on 885⅔ units of thread, $44.44;

The Artistic Weaving Company, processing tax on 38,897 cotton labels, $14.45.

VII

The plaintiff was compelled by the terms of its agreements with said subcontractors to pay the above set forth processing taxes to the subcontractors; by reason of the provisions of the contract, set forth hereinabove in Paragraph IV between the plaintiff and the Government, the amount representing the said processing taxes became an increased charge to the Government under the contract, and has never been paid but on the contrary has been withheld from the plaintiff without just cause.

VIII

The total amount of indebtedness owed the plaintiff by the United States by reason of the payment of processing taxes to subcontractors assessed under the Agricultural Adjustment Act against said subcontractors as shown by the aforesaid allegation of facts is $4,484.43.

IX

The plaintiff submitted its claim to the War Department which was subsequently referred to the Comptroller General of the United States. The claim was finally denied by the said
6 Comptroller General of the United States in his decision of August 11, 1938, A–68085. This petition is respectfully submitted as an appeal from that decision on the grounds that said decision was erroneously given.

X

Your plaintiff is not afforded an appeal to any other department of the Executive Branch of the Government respecting this claim. No action upon this claim, other than that herein stated, excepting that referred to, has been taken before Congress or any of the departments of the United States, or in any Court other than the petition filed in this Court.

XI

Your plaintiff has at all times, through its officers and agents, borne true allegiance to the Government of the United States, and has not in any way voluntarily aided, abetted, or given encouragement to rebellion against said Government. Your plaintiff is the sole and absolute owner of the claim herewith presented, and has made no transfer or assignment of said claim or any part thereof, and is justly entitled to the amount claimed herein from the United States after allowing all just credits and set-offs.

XII

Your plaintiff believes the facts as herein stated are true.

Wherefore, your plaintiff prays judgment in its favor against the United States of America in the sum of $4,484.43 for monies wrongfully withheld from it and for interest at 6% per
7 annum from August 11, 1938, to date of payment, and for

such other and further relief as in the premises to this Court may seem meet and proper.

PHIL D. MORELOCK,
630 Shoreham Building, Washington, D. C.
Attorney for Plaintiff.

Of Counsel:
GEORGE P. LAMB,
630 Shoreham Building, Washington, D. C.
[*Duly sworn to by Phil D. Morelock, jurat omitted in printing.*]

8 II. *General traverse*

Filed January 10, 1939

And now comes the Attorney General, on behalf of the United States, and answering the petition of the claimant herein, denies each and every allegation therein contained; and asks judgment that the petition be dismissed.

JAMES W. MORRIS,
Assistant Attorney General.

G. P.
F. K. D.

III. *Argument and submission of case*

On March 5, 1940, the case was argued and submitted on merits by Mr. Phil D. Morelock for plaintiff, and by Mr. Guy Patten for defendant.

9 IV. *Special findings of fact, conclusion of law, and opinion of the court by Whitaker, J.*

Filed April 1, 1940

Mr. Phil D. Morelock for the plaintiff. George P. Lamb was on the brief.

Mr. Guy Patten, with whom was Mr. Assistant Attorney General Samuel O. Clark, Jr., for the defendant. Messrs. Robert N. Anderson and Fred K. Dyar were on the brief.

This case having been heard by the Court of Claims, the court, upon the basis of a stipulation of facts entered into between the parties, which is all the evidence introduced, makes the following

Special findings of fact

1. Plaintiff is a corporation organized and existing under the laws of the State of Missouri, with its principal offices and place of business at 412 West 8th Street, Kansas City, Missouri.

2. Plaintiff entered into a contract, No. W–669–qm–4800 (O. I. 2538), with the United States through the proper purchasing officer of the Quartermaster Corps, at Philadelphia, Pennsylvania, on June 24, 1933, in which the plaintiff agreed to sell to the United States and deliver at the Quartermaster Depot in Philadelphia, Pennsylvania, 23,496 suits, mechanics type B–1 @ $1.90, for which the United States agreed to pay $44,642.40. Pursuant to a change order dated July 5, 1933, under and by virtue of the provisions of Article 7 of said contract, the total was increased upon written order from the contracting officer of the War Department, and the plaintiff was required to and did supply 11,724 additional suits, mechanics type B–1 @ $1.90, for which the United States agreed to pay $22,275.60. The total number of suits furnished under the contract was 35,220, at an aggregate price of $66,918, which suits were accepted and approved by defendant and said sum of $66,918 has heretofore been paid to plaintiff as by said contract provided.

3. The contract of June 24, 1933, was made pursuant to a bid submitted to the War Department by the plaintiff June 6, 1933. Both the bid and the contract contained the following provision:

"Prices set forth herein include any Federal Tax heretofore imposed by the Congress which is applicable to the material purchased under this contract. If any sales tax, processing tax, adjustment charge, or other taxes or charges are imposed or changed by the Congress after the date set for the opening of the bid upon which this contract is based and made applicable directly upon the production, manufacture, or sale of the supplies covered by this contract and are paid by the contractor on the articles or supplies herein contracted for, then the prices named in this contract will be increased or decreased accordingly and any amount due the contractor as a result of such change will be charged to the government and entered on vouchers (or invoices) as separate items."

4. Plaintiff manufactured the suits involved in the aforesaid contract, and in the manufacture thereof it used 213,127¾ yards of cotton cloth which it purchased from McCampbell and Company, 320 Broadway, New York, selling agent for Graniteville Manufacturing Company of South Carolina, a first domestic processor of cotton.

The confirmation by McCampbell and Company of plaintiff's order, dated June 23, 1933, for the aforesaid cotton cloth contained the following provision:

"The prices stated herein are based upon present manufacturing conditions and cost thereunder. If such cost is increased by any Federal taxes or by the administration of the Industrial

Recovery Act, the Agricultural Adjustment Act, or by any Federal regulations or Federally approved codes and practices, affecting costs, not now in force, the amount of such in-
11 creased cost shall be added to the prices stated and delivery shall be extended in proportion to any limitation of production caused thereby."

Pursuant to the above provision, McCampbell and Company billed plaintiff, as a separate item in its invoices for the above-mentioned cotton cloth, for the amount of tax applicable to the processing of the cotton from which said cloth was manufactured, to-wit, the sum of $4,425.54, which amount plaintiff paid to McCampbell and Company. Processing taxes in the same amount were paid by Graniteville Manufacturing Company, the processor, to the Collector of Internal Revenue, which amount was included in larger amounts of processing taxes paid by said processor.

5. In manufacturing the aforesaid suits, plaintiff used 885⅔ units of cotton thread which it purchased from American Thread Company, a first domestic processor of cotton. The confirmation by American Thread Company of plaintiff's order, dated June 24, 1933, for said cotton thread, contained the following provision:

"In addition to the prices upon which this contract of sale is based, buyer agrees to pay any additional costs resulting from any sales tax or taxes and/or domestic allotment charges that may be imposed by the Federal, State, and/or local government and applicable to any items on this contract at time of shipment."

Pursuant to the above provision, American Thread Company, a first domestic processor of cotton, billed plaintiff, as a separate item in its invoices for the above-mentioned cotton thread, for the amount of tax applicable to the processing of cotton from which said thread was manufactured, to-wit, the sum of $44.44, which amount plaintiff paid to American Thread Company. Processing taxes in the same amount were paid by American Thread Company, the processor, to the Collector of Internal Revenue, which amount was included in larger amounts of processing taxes paid by said processor.

6. Plaintiff duly made claim and demand against the United States, with the War Department, that the contract price for the mechanics suits be increased by the sum of $4,469.98,
12 being the processing tax applicable to the processing of the cotton used in manufacturing and processing the supplies which plaintiff purchased and used, as aforesaid, to manufacture said mechanics suits.

The claim was referred, subsequently, to the Comptroller General of the United States, and was denied and rejected by said Comptroller General in his decision of August 11, 1936, A–68085.

7. The Secretary of Agriculture, in accordance with authority vested in him by the provisions of the Agricultural Adjustment Act of May 12, 1933 (48 Stat. 31), as amended, for the purposes of said Act, prescribed that the first marketing year for cotton began August 1, 1933, and fixed the rate of tax at 4.2 cents per pound beginning August 1, 1933. The processing taxes of $4,469.98 were assessed and paid subsequent to the contracts entered into between the plaintiff and the War Department and subsequent to the agreements between the plaintiff and the processors.

8. Plaintiff is the sole owner of the claim sued upon, and has never transferred the same, or any part thereof, or any interest therein, and no action other than herein stated has been had on said claim through Congress, or in any of the Departments of the Government.

Conclusion of law

Upon the foregoing special findings of fact, which are made a part of the judgment herein, the Court decides as a conclusion of law that the plaintiff is entitled to recover the sum of $4,469.98.

It is therefore ordered and adjudged that the plaintiff recover of and from the United States the sum of four thousand four hundred sixty-nine dollars and ninety-eight cents ($4,469.98).

Opinion

WHITAKER, Judge, delivered the opinion of the court:

The plaintiff entered into a contract with the defendant on June 24, 1933, to furnish a certain number of suits of a certain type for a specified price. The contract entered into
13 contained the following provision, known as the "Federal Taxes" provision:

"Prices set forth herein include any Federal Tax heretofore imposed by the Congress which is applicable to the material purchased under this contract. If any sales tax, processing tax, adjustment charge, or other taxes or charges are imposed or changed by the Congress after the date set for the opening of the bid upon which this contract is based and made applicable directly upon the production, manufacture, or sale of the supplies covered by this contract and are paid by the contractor on the articles or supplies herein contracted for, then the prices named in this contract will be increased or decreased accordingly and any amount due the contractor as a result of such change will be

charged to the government and entered on vouchers (or invoices) as separate items."

In order to carry out its contract the plaintiff purchased cotton cloth and cotton thread at a certain price, plus the amount of any taxes levied by the Industrial Recovery Act, the Agricultural Adjustment Act, and others. After the purchase of the cloth and thread the vendors thereof paid processing taxes thereon in the total amount of $4,469.98, for which amount they were reimbursed by the plaintiff. The plaintiff then made demand on the defendant for an additional payment to it of this amount under the "Federal Taxes" provision of its contract. The claim was denied and this suit was brought.

The defendant defends on the ground that the Agricultural Adjustment Act was passed prior to the date of plaintiff's contract and, therefore, under the "Federal Taxes" provision of the contract plaintiff is not entitled to any additional payment on account of the taxes levied by that Act. That provision recites that the prices set forth therein include any Federal tax "heretofore imposed by the Congress," but the defendant agreed to pay an additional sum to the contractor in case any processing tax, among others, is "imposed or changed by the Congress *after* the date set for the opening of the bid upon which this contract is based." [Italics ours.]

While the Agricultural Adjustment Act was passed prior to the date of the contract, it did not definitely provide for
14 any tax on the processing of cotton, nor did it specify the amount thereof, if one should be imposed, nor when it should become effective. Its provisions with respect to a processing tax on cotton are as follows:

In section 2 (1) Congress declared that it was its purpose in passing the Act, among others,

"To establish and maintain such balance between the production and consumption of agricultural commodities, and such marketing conditions therefor, as will reestablish prices to farmers at a level that will give agricultural commodities a purchasing power with respect to articles that farmers buy equivalent to the purchasing power of agricultural commodities in the base period."

In section 8 the Secretary of Agriculture is given power, in order to effectuate the declared policy, to provide, among other things, for reduction in the acreage of any basic agricultural commodity, and "to provide for rental or benefit payments in connection therewith * * * in such amounts as the Secretary deems fair and reasonable."

In section 9 (a) it is provided:

"When the Secretary of Agriculture determines that rental or benefit payments are to be made with respect to any basic

agricultural commodity, he shall proclaim such determination, and a processing tax shall be in effect with respect to such commodity from the beginning of the marketing year therefor next following the date of such proclamation. * * * The rate of tax shall conform to the requirements of subsection (b)."

In subsection (b) it is provided:

"The processing tax shall be at such rate as equals the difference between the current average farm price for the commodity and the fair exchange value of the commodity; * * *"

unless the Secretary concludes that the tax at such rate would cause an accumulation of surplus stocks or a depression of the farm price of the commodity, in which event it is provided that "the processing tax shall be at such rate as will prevent such accumulation of surplus stocks and depression of the farm price of the commodity."

15 From the foregoing quotations from the Act it is obvious that with respect to cotton, for instance, it was unknown after the passage of the Act whether or not there would be any processing tax with respect thereto. Whether or not there should be was dependent upon the future action of the Secretary of Agriculture. No processing tax on cotton became effective until the Secretary had determined that rental or benefit payments should be made with respect thereto. Whether or not he would ever make such determination was unknown, although it might reasonably have been anticipated. But even so, it was impossible to determine from the Act when the tax should become effective, since it would not become effective until the beginning of the marketing year after such determination of the Secretary. The plaintiff, therefore, did not know when it entered into its contract whether or not it would have to pay any processing taxes.

Nor could the rate of the tax be determined from the Act. The Act authorized the Secretary of Agriculture to determine the rate at such amount as would equalize the current average farm price of the commodity and the fair exchange value of the commodity. The plaintiff manifestly was unable to tell therefrom what rate the Secretary would fix. Moreover, the Secretary was not bound by this formula if he believed that its application would result in an accumulation of surplus stocks of the commodity or in the depression of its price. In this event he was authorized to fix a different rate, one that would prevent such accumulation of stocks or depression of price.

Even after the rate had been fixed by the Secretary, he had the right under the Act to vary it from time to time if he found this necessary in order to effectuate the declared purpose of Congress in passing the Act.

It is manifest, therefore, that it was impossible for either the plaintiff or its vendors to have determined the amount of the tax which it would be necessary to pay.

Under such circumstances we cannot say that these taxes had been "imposed" prior to the date of plaintiff's contract with the defendant, within the meaning in which that word was used in the contract. Authority had been conferred by
16 Congress for the imposition of the tax, but that authority had not been exercised until thereafter, to wit, on July 14, 1933. The purpose of the Federal Taxes provision of the contract was to reimburse the contractor for its additional costs brought about by the defendant's act in levying additional taxes. The taxes were not in effect when the contract was made and it was impossible for the contractor to ascertain when they would go into effect or the amount of them when they did. Therefore it could not figure what to include in its costs on account of them.

We are, therefore, of opinion that the processing taxes paid by the plaintiff were taxes "imposed or changed by the Congress after the date set for the opening of the bid upon which this contract is based." The action of Congress in imposing the tax was not complete until action by its delegate, the Secretary of Agriculture, and this was after the contract was made.

All other questions raised by the defendant have been disposed of by our decisions in Batavia Mills, Inc., v. The United States, 85 Ct. Cls., 447, and The Telescope Folding Furniture Company, Inc., v. The United States, decided March 4, 1940.

It results that plaintiff is entitled to recover of the defendant the sum of $4,469.98. It is so ordered.

LITTLETON, Judge; GREEN, Judge; and WHALEY, Chief Justice, concur.

WILLIAMS, Judge, took no part in the decision of this case.

17 V. *Judgment*

At a Court of Claims held in the City of Washington on the 1st day of April, A. D. 1940, judgment was ordered to be entered as follows:

Upon the special findings of fact, which are made a part of the judgment herein, the court decides, as a conclusion of law, that the plaintiff is entitled to recover the sum of $4,469.98.

It is therefore adjudged and ordered that the plaintiff recover of and from the United States the sum of four thousand four hundred sixty-nine dollars and ninety-eight cents ($4,469.98).

18 [Clerk's certificate to foregoing transcript omitted in printing.]

[Endorsement on cover:] Enter Attorney General. File No. 44537. Court of Claims. Term No. 188. The United States, Petitioner vs. Cowden Manufacturing Company. Petition for writ of certiorari and exhibit thereto. Filed June 27, 1940. Term No. 188 O. T. 1940.

U. S. GOVERNMENT PRINTING OFFICE: 1940

Supreme Court of the United States

Order allowing certiorari

Filed October 14, 1940

The petition herein for a writ of certiorari to the Court of Claims is granted. And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

U. S. GOVERNMENT PRINTING OFFICE: 1940

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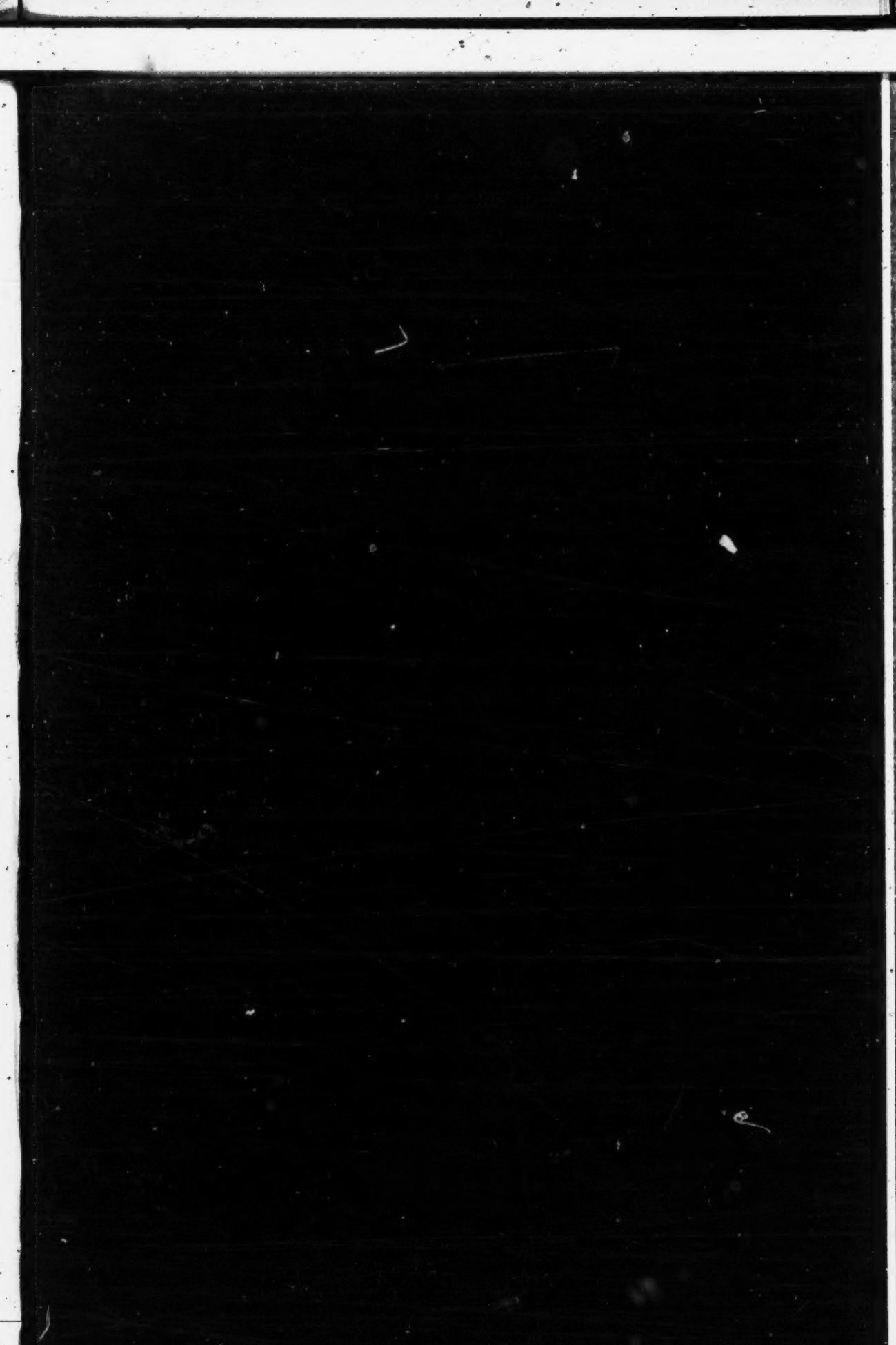

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In the Supreme Court of the United States

OCTOBER TERM, 1940

No. ——

THE UNITED STATES, PETITIONER

v.

COWDEN MANUFACTURING COMPANY

PETITION FOR A WRIT OF CERTIORARI TO THE COURT OF CLAIMS

The Solicitor General, on behalf of the United States, prays that a writ of certiorari issue to review the judgment of the Court of Claims entered in the above-entitled cause.

OPINION BELOW

The opinion of the Court of Claims (R. 12) is reported in 32 F. Supp. 141.

JURISDICTION

The judgment of the Court of Claims was entered on April 1, 1940. (R. 17.) The jurisdiction of this Court is invoked under Section 3 (b) of the Act of February 13, 1925, as amended by the Act of May 22, 1939.

QUESTION PRESENTED

Respondent contracted to sell to the United States a specified number of mechanic's suits at a stated price. The contract provided for the addition to the purchase price of any after-imposed federal taxes which might be "made applicable directly upon the * * * manufacture * * * of the supplies covered by this contract" and which "are paid by the contractor on the articles or supplies herein contracted for".

In purchasing cloth and thread to be used in manufacturing the suits, respondent was compelled to reimburse its vendors for processing taxes paid by them in producing these materials. Is respondent entitled to add such extra costs to the contract price in its sales of the suits to the United States?

STATUTE INVOLVED

The pertinent provisions of the Agricultural Adjustment Act, c. 25, 48 Stat. 31, are as follows:

PROCESSING TAX

SEC. 9. (a) To obtain revenue for extraordinary expenses incurred by reason of the national economic emergency, there shall be levied processing taxes as hereinafter provided. When the Secretary of Agriculture determines that rental or benefit payments are to be made with respect to any basic agricultural commodity, he shall proclaim such determination, and a processing tax shall be in effect with respect to such com-

modity from the beginning of the marketing year therefor next following the date of such proclamation. The processing tax shall be levied, assessed, and collected upon the first domestic processing of the commodity, whether of domestic production or imported, and shall be paid by the processor. The rate of tax shall conform to the requirements of subsection (b) * * *.

* * * * *

(d) As used in part 2 of this title—

* * * * *

(2) In case of cotton, the term "processing" means the spinning, manufacturing, or other processing (except ginning) of cotton; * * *

STATEMENT

The special findings of fact of the Court of Claims may be summarized as follows:

Respondent, a Missouri corporation, entered into a contract with the United States through the proper purchasing officer of the Quartermaster Corps at Philadelphia, Pennsylvania, on June 24, 1933, under the amended terms of which respondent agreed to sell to the United States 35,220 suits, mechanics type B–1, at $1.90 each, or a total of $66,918. The suits were delivered to and accepted by the petitioner and the sum of $66,918 was paid to the respondent. (R. 9, 10.)

The contract in question was made pursuant to a bid submitted to the War Department by the

respondent on June 6, 1933. Both the bid and the contract contained the following provision (R. 10):

> Prices set forth herein include any Federal tax heretofore imposed by the Congress which is applicable to the material purchased under this contract. If any sales tax, processing tax, adjustment charge, or other taxes or charges are imposed or changed by the Congress after the date set for the opening of the bid upon which this contract is based and made applicable directly upon the production, manufacture, or sale of the supplies covered by this contract and are paid by the contractor on the articles or supplies herein contracted for, then the prices named in this contract will be increased or decreased accordingly and any amount due the contractor as a result of such change will be charged to the government and entered on vouchers (or invoices) as separate items.

Respondent purchased the cotton cloth from which it manufactured the suits in question from McCampbell and Company, 320 Broadway, New York, selling agent for Graniteville Manufacturing Company of South Carolina, under a contract providing for increasing the price of the cotton by the amount of any federal taxes imposed after the contract date and before delivery of the cloth. Pursuant to this provision McCampbell and Company billed respondent as a separate item on the invoices for the cloth in question in the amount of $4,425.54, covering processing taxes paid by the first proces-

sor of the cloth to the Collector of Internal Revenue. (R. 10, 11.)

In the manufacture of the suits respondent also used a substantial quantity of cotton thread purchased from American Thread Company under a contract containing a provision similar to that heretofore referred to, as a result of which respondent paid to American Thread Company $44.44, covering processing taxes paid by that company to the Collector of Internal Revenue on the thread in question. (R. 11,)

Respondent filed a claim against the United States with the War Department for the amount of $4,469.98, being the aggregate processing tax applicable to the cotton cloth and thread used in the manufacture of the suits. The claim was referred to the Comptroller General of the United States and was rejected by him on August 11, 1936. (R. 11–12.)

On December 1, 1938, this suit was filed in the Court of Claims, which rendered an opinion in favor of the respondent and entered judgment in the amount of $4,469.98. (R. 1, 9, 17.)

SPECIFICATION OF ERRORS TO BE URGED

The court below erred:

1. In holding that respondent is entitled to reimbursement under the terms of the contract for taxes ultimately borne by it but paid by the first processors of the materials used by respondent in the manufacture of the supplies covered by the contract.

2. In failing and refusing to hold that the taxes were not "made applicable directly upon the production, manufacture or sale of the supplies" covered by the contract and were not "paid by the contractor on the articles or supplies" contracted for.

3. In holding that the taxes involved were "imposed or changed by the Congress after the date set for the opening of the bid".

4. In failing to enter judgment for the United States and dismiss the petition.

REASONS FOR GRANTING THE WRIT

1. The decision below conflicts in principle with *United States* v. *Glenn L. Martin Co.*, 308 U. S. 62, and presents a question of general importance. That case involved the application of a substantially identical contractual provision to taxes imposed by the Social Security Act. This Court stressed the fact that the taxes must be "on" the articles sold to the United States. (P. 65.) Here, the articles sold to the United States were articles of clothing, and the taxes in question were imposed, not upon the manufacture of those articles, but upon the prior manufacture of the cloth and thread. Indeed, the instant case is an even stronger one for the Government than the *Glenn L. Martin Co.* case, for the taxes there were imposed in connection with the manufacture of the very products that were sold to the United States.

The conflict with the *Glenn L. Martin Co.* case is emphasised by the further requirement in the contract that the taxes must be "paid by the contractor on the articles or supplies herein contracted for". (R. 10.) Plainly, respondent did not become a taxpayer merely by reimbursing its vendors for processing taxes which they had paid. *Oswald Jaeger Baking Co.* v. *Commissioner,* 108 F. (2d) 375 (C. C. A. 7th), certiorari denied, April 1, 1940, No. 771, 1939 Term. The only reasonable interpretation of this language is that the contractor seeking reimbursement must have been the taxpayer and that the tax must have been paid on the finished product sold to the Government. The practical difficulties of tracing taxes imposed at some anterior stage upon the processing of the raw materials employed in producing the finished product preclude the contrary view.[1]

[1] The opinion of the Court of Claims did not consider in detail the issue upon the basis of which we are asking for certiorari. It discussed only whether the taxes in question were "imposed or changed by the Congress after the date set for the opening of the bid" within the meaning of the contract in the light of the fact that the Agricultural Adjustment Act was enacted *before* that date. The Government had contended that the mere fact that the imposition of the taxes was delayed until after the proclamation of the Secretary of Agriculture which occurred after the critical date did not convert them into taxes "imposed * * * *by the Congress*" after that date.

The question that we raise here was fully briefed and argued, but it was summarily disposed of by the Court of Claims by reference to its earlier decisions in *Batavia Mills, Inc.* v. *United States,* 85 C. Cls. 447, and *Telescope Folding*

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No. 15

Supreme Court of the United States

OCTOBER TERM, 1940

THE UNITED STATES, PETITIONER

v.

CROWELL MANUFACTURING COMPANY

PETITION FOR WRIT OF CERTIORARI TO THE COURT OF CLAIMS

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In the Supreme Court of the United States

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No. 188

THE UNITED STATES, PETITIONER

v.

COWDEN MANUFACTURING COMPANY

ON WRIT OF CERTIORARI TO THE COURT OF CLAIMS

BRIEF FOR THE UNITED STATES

OPINION BELOW

The opinion of the Court of Claims (R. 5) is reported in 32 F. Supp. 141.

JURISDICTION

The judgment of the Court of Claims was entered on April 1, 1940 (R. 11). The petition for a writ of certiorari was filed June 27, 1940 (R. 12), and was granted October 14, 1940. The jurisdiction of this Court rests on Section 3 (b) of the Act of February 13, 1925, as amended by the Act of May 22, 1939.

QUESTION PRESENTED

Respondent contracted to sell to the United States a specified number of mechanics' suits at a stated price. The contract provided for the addition to the purchase price of any after-imposed federal taxes which might be "made applicable directly upon the * * * manufacture * * * of the supplies covered by this contract" and which "are paid by the contractor on the articles or supplies herein contracted for".

In purchasing cloth and thread to be used in manufacturing the suits, respondent was compelled to reimburse its vendors for processing taxes paid by them in producing these materials. Is respondent entitled to add such extra costs to the contract price in its sales of the suits to the United States?

STATUTE INVOLVED

The pertinent provisions of the Agricultural Adjustment Act, c. 25, 48 Stat. 31, are as follows:

PROCESSING TAX

> SEC. 9. (a) To obtain revenue for extraordinary expenses incurred by reason of the national economic emergency, there shall be levied processing taxes as hereinafter provided. When the Secretary of Agriculture determines that rental or benefit payments are to be made with respect to any basic agricultural commodity, he shall proclaim such determination, and a processing tax shall be in effect with respect to

such commodity from the beginning of the marketing year therefor next following the date of such proclamation. The processing tax shall be levied, assessed, and collected upon the first domestic processing of the commodity, whether of domestic production or imported, and shall be paid by the processor. The rate of tax shall conform to the requirements of subsection (b). * * * .

* * * * *

(d) As used in part 2 of this title—

* * * * *

(2) In case of cotton, the term "processing" means the spinning, manufacturing, or other processing (except ginning) of cotton; * * * .

STATEMENT

The special findings of fact of the Court of Claims may be summarized as follows:

Respondent, a Missouri corporation, entered into a contract with the United States through the proper purchasing officer of the Quartermaster Corps at Philadelphia, Pennsylvania, on June 24, 1933, under the amended terms of which respondent agreed to sell to the United States 35,220 suits, mechanics type B–1, at $1.90 each, or a total of $66,918. The suits were delivered to and accepted by the petitioner and the sum of $66,918 was paid to the respondent. (R. 5, 6.)

The contract in question was made pursuant to a bid submitted to the War Department by the

respondent on June 6, 1933. Both the bid and the contract contained the following provision (R. 6):

> Prices set forth herein include any Federal Tax heretofore imposed by the Congress which is applicable to the material purchased under this contract. If any sales tax, processing tax, adjustment charge, or other taxes or charges are imposed or changed by the Congress after the date set for the opening of the bid upon which this contract is based and made applicable directly upon the production, manufacture, or sale of the supplies covered by this contract and are paid by the contractor on the articles or supplies herein contracted for, then the prices named in this contract will be increased or decreased accordingly and any amount due the contractor as a result of such change will be charged to the government and entered on vouchers (or invoices) as separate items.

Respondent purchased the cotton cloth from which it manufactured the suits in question from McCampbell and Company, 320 Broadway, New York, selling agent for Graniteville Manufacturing Company of South Carolina, under a contract providing for increasing the price of the cotton by the amount of any federal taxes imposed after the contract date and before delivery of the cloth. Pursuant to this provision McCampbell and Company billed respondent as a separate item on the invoices for the cloth in question in the amount of $4,425.54,

covering processing taxes paid by the first processor of the cloth to the Collector of Internal Revenue. (R. 6–7.)

In the manufacture of the suits respondent also used a substantial quantity of cotton thread purchased from American Thread Company under a contract containing a provision similar to that heretofore referred to, as a result of which respondent paid to American Thread Company $44.44, covering processing taxes paid by that company to the Collector of Internal Revenue on the thread in question. (R. 7.)

Respondent filed a claim against the United States with the War Department for the amount of $4,469.98, being the aggregate processing tax applicable to the cotton cloth and thread used in the manufacture of the suits. The claim was referred to the Comptroller General of the United States and was rejected by him on August 11, 1936. (R. 7–8.)

On December 1, 1938, this suit was filed in the Court of Claims, which rendered an opinion in favor of the respondent and entered judgment in the amount of $4,469.98. (R. 1, 5–11.)

SPECIFICATION OF ERRORS TO BE URGED

The court below erred:

1. In holding that respondent is entitled to reimbursement under the terms of the contract for "taxes" ultimately borne by it but paid by the

first processors of the materials used by respondent in the manufacture of the supplies covered by the contract.

2. In failing and refusing to hold that the taxes were not "made applicable directly upon the production, manufacture, or sale of the supplies" covered by the contract and were not "paid by the contractor on the articles or supplies" contracted for.

3. In failing to enter judgment for the United States and dismiss the petition.

SUMMARY OF ARGUMENT

Respondent may add to the contract price only such taxes as were "applicable directly upon the production, manufacture, or sale of the supplies" covered by the contract. The "supplies" here were mechanics suits, and no tax whatever was imposed with respect to the production, manufacture, or sale of mechanics suits. The taxes which respondent seeks to add to the contract price were imposed upon the processors of the cotton and thread purchased by respondent. Not only were these taxes *not* "applicable directly upon the * * * manufacture * * *" of the mechanics suits; they were not even imposed upon respondent. Moreover, respondent's mere reimbursement of taxes paid by another did not make it a taxpayer.

ARGUMENT

THE CONTRACT DOES NOT PROVIDE FOR REIMBURSEMENT OF THE PROCESSING TAXES HERE SOUGHT

The contract here in question provides that the specified prices are to be altered only to reflect taxes or charges (R. 6) "imposed or changed by the Congress after the date set for the opening of the bid upon which this contract is based and made applicable directly upon the production, manufacture, or sale of the supplies covered by this contract and * * * paid by the contractor on the articles or supplies herein contracted for, * * *."

The taxes for which respondent seeks to be reimbursed were not imposed upon it. They were imposed under Section 9 of the Agricultural Adjustment Act upon the processors of the cotton and thread which respondent purchased. They were not imposed with respect to respondent's manufacturing operations in converting the cotton and thread into mechanics' suits. Rather, the taxes were laid with respect to the manufacturing operations of respondent's vendors.

Under respondent's contract with the United States the taxes may be included in the contract price only if they are "applicable directly upon the production, manufacture, or sale of the supplies covered by" the contract. (R. 6.) But the "supplies" covered by the contract in this case were mechanics' suits, not cotton or thread. And no tax

of any kind, directly or indirectly, was imposed with respect to the "production, manufacture, or sale" of mechanics' suits.[1]

That respondent's mere reimbursement of taxes imposed upon and paid by its vendors does not come within the contract provision is, we submit, plain, and follows *a fortiori* from *United States* v. *Glenn L. Martin Co.*, 308 U. S. 62. That case involved a contractual provision substantially identical with the one in controversy here, and the question there was whether Social Security taxes imposed upon the contracting corporation itself could be added to the contract price. In denying the claimant's contention, this Court stressed the fact that the taxes must be "on" the article sold to the Government. (P. 65.) In the instant case, the taxes certainly were not imposed "on" the mechanics' suits. Indeed they were not even imposed

[1] The instant case is thus to be distinguished from *Batavia Mills, Inc.* v. *United States*, 85 C. Cls. 447, relied upon by respondent. There, the contractor had undertaken to sell certain supplies to the United States, and had purchased those supplies completely fabricated. The contractor reimbursed the vendor for the taxes paid with respect to the production of those supplies, and was permitted to add such taxes to the contract price. Thus, the taxes in that case were levied with respect to the very subject matter of the contract with the United States, whereas here the taxes were imposed in connection with the processing of the constituent raw materials that went to make up the final product. And, in any event, the decision reached in the *Batavia Mills* case rests upon exceedingly dubious grounds.

upon the contractor.[2] They were imposed upon the processors of the raw materials that were purchased and employed by the contractor in producing its final product for sale to the Government. And the mere reimbursement of those taxes by the contractor to its vendors does not render it a taxpayer. *Oswald Jaeger Baking Co.* v. *Commissioner,* 108 F. (2d) 375 (C. C. A. 7th), certiorari denied, 309 U. S. 683; *Zinsmaster Baking Co.* v. *Commissioner,* 109 F. (2d) 738 (C. C. A. 8th); *New Consumers Bread Co.* v. *Commissioner* (C. C. A. 3d), decided October 4, 1940; *Fuhrman & Forster Co.* v. *Commissioner* (C. C. A. 7th), decided, July 22, 1940. Cf. *Lash's Products Co.* v. *United States,* 278 U. S. 175.

That reimbursement of the character here sought was not contemplated by the parties is apparent not only from the precise use of the word "directly," but from the general character of the tax provision. While they might have contracted to do business on a cost-plus basis, or might have in-

[2] Some of the cases dealing with intergovernmental tax immunity, while not squarely in point, furnish a persuasive analogy. On the assumption that the test of immunity was whether the burden was direct or indirect, the Court in *Liggett & Myers Co.* v. *United States,* 299 U. S. 383, 386, held that a tax on the manufacture of tobacco subsequently sold to a state instrumentality did not impose any "direct burden" upon the state. And in *Wheeler Lumber Co.* v. *United States,* 281 U. S. 572, 579, the Court held that a federal tax on the transportation of lumber sold to a county was valid since "the transportation was not part of the sale but preliminary to it and wholly the vendor's affair."

cluded an "equitable adjustment" clause as is done in many government contracts, the parties provided only for price increases to reflect taxes imposed "directly" on the manufacture of the contract articles. Cf. *Cramp & Sons Ship Co.* v. *United States*, 72 C. Cls. 146.

Not only is the construction here urged that contemplated by the parties, but it represents the only reasonable interpretation of the provisions of the contract. Any other construction introduces the difficult, and in many instances impossible, task of tracing the shifting burden of taxes to determine where it has ultimately fallen. The preference in the construction of contracts for an interpretation avoiding unreasonable or impossible results is well established. See Williston, *Contracts* (Rev. ed., 1936), 1786 ff.

CONCLUSION

The decision of the court below is erroneous and should be reversed.

Respectfully submitted.

FRANCIS BIDDLE,
Solicitor General.
SAMUEL O. CLARK, JR.,
Assistant Attorney General.
J. LOUIS MONARCH,
ANDREW D. SHARPE,
HUBERT WILL,
Special Assistants to the Attorney General.

NOVEMBER 1940.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1940

No. 188

THE UNITED STATES, *Petitioner,*

v.

COWDEN MANUFACTURING COMPANY

On Petition for a Writ of Certiorari to the Court of Claims of the United States.

BRIEF FOR THE RESPONDENT IN OPPOSITION.

PHIL D. MORELOCK,
Attorney for Respondent.

PRESS OF BYRON S. ADAMS, WASHINGTON, D. C.

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BRIEF FOR THE RESPONDENT IN OPPOSITION.

Opinion Below.

The opinion of the Court of Claims (R. 12) is reported in 33 F. Supp. 141.

Jurisdiction.

The judgment of the Court of Claims was entered April 1, 1940 (R. 17). The petition for writ of certiorari was filed June 27, 1940. Service was had and acknowledged by

the respondent on July 17, 1940. The jurisdiction of this court is invoked under Section 3(b) of the Act of February 13, 1925, as amended by the Act of May 22, 1939.

Question Presented.

Where respondent contracted to sell to the United States mechanics suits at a certain price and the contract provided for reimbursement to respondent for any processing taxes imposed upon the materials or supplies used by the respondent in fulfilling its contract, and,

Where processing taxes were imposed on the materials subsequent to the date of the contract, billed to and paid by the respondent to the manufacturer as a separate item,

Is the respondent entitled to recover under the terms of the contract from the United States the amount of the processing taxes paid to the manufacturer of the materials upon which the taxes were imposed?

Statement.

Respondent is a Missouri corporation with officers at 412 West 8th Street, Kansas City, Missouri (R. 9).

On June 24, 1933, pursuant to a bid submitted on June 6, 1933, it entered into a contract, No. W-699-qm-4800 (O. I. 2538), with the United States through the proper purchasing officers of the Quartermaster Corps at Philadelphia, Pennsylvania, in which respondent agreed to sell to the United States and deliver at the Quartermaster Depot at Philadelphia, Pennsylvania, 23,496 suits, mechanics type B-1 at $1.90 for which the United States agreed to pay $44,642.40. In accordance with a change order dated July 5, 1933, under article 7 of the contract, the total was increased upon written order from the proper contracting officer of the War Department and respondent was required to and did furnish 11,724 additional suits, mechanics type B-1 at $1.90 for which the United States agreed to pay $22,275.60. All suits, totalling 35,220, were delivered by

the respondent, accepted and approved by the United States, and $66,918.00 paid by the United States to the respondent as provided by the contract. (R. 9-10)

Both the bid made June 6, 1933, and the contract of June 24, 1933, contained the following provision:

> "Prices set forth herein include any Federal Tax heretofore imposed by the Congress which is applicable to the material purchased under the contract. If any sales tax, processing tax, adjustment charge or other taxes or charges are imposed or changed by the Congress after the date set for the opening of the bid upon which this contract is based, and made applicable directly upon the production, manufacture, or sale of the supplies covered by this contract and are paid by the contractor on the articles or supplies herein contracted for, then the prices named in this contract will be increased or decreased accordingly and any amount due the contractor as a result of such change, will be charged to the Government and entered on vouchers (or invoices) as separate items." (R. 10)

Respondent, in the manufacture of the suits, used 213,127¾ yards of cotton cloth purchased from McCampbell and Company, 320 Broadway, New York, selling agents for the Graniteville Manufacturing Company of South Carolina, a first domestic processor. Also respondent used 885-2/5 units of cotton thread purchased from the American Thread Company. The confirmation of respondent's orders for these materials by McCampbell and Company under date of June 23, 1933, and the American Thread Company, dated June 24, 1933, contained clauses to the effect that any Federal Taxes imposed after the confirmation upon the materials would be in addition to the prices quoted. (R. 10-11)

Pursuant to the provisions in the confirmations, McCampbell and Company billed the respondent as a separate item for processing tax in the amount of $4,425.54 and the American Thread Company billed the respondent as a separate item for processing taxes in the amount of $44.44. These

taxes were paid by the respondent to the processors and in turn by them paid to the Collector of Internal Revenue. (R. 11)

Respondent duly made claim and demand against the United States with the War Department for an increase in its contract price of $4,469.98 which was the processing tax imposed upon the processing of the cotton used in the manufacture of the cloth purchased and used by the respondent in the manufacture of the mechanics suits furnished by the respondent to the United States. (R. 11-12)

Thereafter, the claim was referred to the Comptroller General of the United States and was denied and rejected by the Comptroller General in his decision dated August 11, 1936, A-68085. (R. 12)

The Secretary of Agriculture, pursuant to authority vested in him by the provisions of the Agricultural Adjustment Act of May 12, 1933 (48 Stat. 31) as amended, prescribed that the first marketing year for cotton began August 1, 1933. The tax was fixed at 4.2 cents per pound beginning August 1, 1933. The processing taxes of $4,469.98 were assessed and paid subsequent to the date of the contracts entered into between the respondent and the War Department and subsequent to the agreements between the respondent and the processors. (R. 12)

This suit was filed December 1, 1938, in the Court of Claims of the United States, which rendered an opinion in favor of and entered judgment for the respondent in the amount of $4,469.98 on April 1, 1940. (R. 1, 9, 17)

Argument.

This was not a suit for the recovery of a tax but an action based upon the provisions of a contract. The respondent entered into the contract with the United States in good faith. The prices contracted for did not include any processing taxes. It was understood by the respondent and was the express provision of the contract that should any processing tax be imposed upon the supplies necessary to use in

the manufacture of the suits which had to be paid by the respondent, then the respondent would accordingly be reimbursed. It was not the intention of the respondent to make any profit with respect to such a tax but merely to be made whole as, if and when such tax was paid, which was provided by the contract. The respondent had every right to expect that it would be reimbursed for the tax which it was forced to pay. *Batavia Mills, Inc.* v. *United States,* 85 Ct. Cls. 447; *Righter* v. *United States,* 85 Ct. Cls. 699; *Telescope Folding Furniture Company* v. *United States,* 31 F. Supp. 780.

The respondent not only did not include the tax which it paid to the processors in its bid and contract price, but such tax could not have been so included because it was unknown as to whether a tax would be imposed upon cotton or, if imposed, as to the amount or measure of such tax. The tax was levied upon the processing of the cotton and paid by the manufacturer which processed the cloth purchased and used by the respondent in the manufacture of the suits furnished to the United States. The processor in turn passed the tax on to the respondent as a specific item. In harmony with the principles laid down in *Lash's Products Company* v. *United States,* 278 U. S. 175, this serves to identify the item which was not absorbed by the manufacturer but was passed on directly to the respondent and is recoverable under the specific provisions of the contract.

By paying the respondent in accordance with the provisions of the contract, the United States is, in effect, merely returning to the respondent the money which was collected from the respondent through the processor as a processing tax which was later voided when the Agricultural Adjustment Act was declared unconstitutional. *United States* v. *Butler,* 297 U. S. 1. Not only has the United States failed to reimburse the respondent in accordance with the contract for the processing tax paid by it on the materials used in the manufacture of the suits but the United States has been unjustly enriched by the collection from the respondent

through the processor of an unconstitutional tax. However, as heretofore stated, this is not a suit to recover a tax but is based upon the provisions of the contract.

The case of *Oswald Jaeger Baking Co.* v. *Commissioner*, 108 F. (2d) 375 (C. C. A. 7th) certiorari denied, April 1, 1940, No. 771, 1939 Term, cited by the petitioner in its brief is not in point. This case involved an appeal from the United States Processing Tax Board of Review, before which, as provided by Title VII of the Revenue Act of 1936 (7 U. S. C. Para. 648), the petitioner had prosecuted a claim for refund for processing taxes after the said claim had been rejected by the Commissioner of Internal Revenue. No contract was involved as in the case at bar.

In support of its petition for a writ of certiorari, the petitioner urges that the decision of the Court of Claims is in conflict with the decision of this Court in *United States* v. *Glenn L. Martin Company*, 308 U. S. 62, hereinafter referred to as the Martin Company. It is respectfully submitted that the position of the respondent is supported by the decision of this Court in the *Martin Company* case in that the respondent's contract with the United States specifically provides for reimbursement to the respondent by the United States of "processing taxes" levied upon the materials used by the respondent in the manufacture of the suits.

The Martin Company contracted with the War Department to furnish aircraft and aircraft materials. The provisions of the contract were substantially identical with the provisions of the contract here under consideration. Subsequent to the date of the contract, the Social Security Act became effective and the State of Maryland enacted an Unemployment Compensation law. The Martin Company paid the United States $794.03 Federal Social Security Taxes and to the State of Maryland $6,943.29 Unemployment Compensation taxes with respect to *payrolls* of employees who were engaged in work on the contracts in 1936 and 1937. The Martin Company sought to recover from

the United States the Social Security taxes and the Unemployment Compensation taxes paid, alleging that such recovery was proper under the terms of the contract.

In denying the right of the Martin Company to recover under its contract, this Court said,

> "Thus, this contract was concerned with Federal taxes 'on' the goods to be provided under it, whatever the occasion for the taxes. And a tax 'on' the relationship of employer-employee—characterized as a tax on payrolls—is not of the type treated by the contract as a tax 'on' the goods or articles sold.
>
> "The contract refers only to Federal taxes, existing or future on 'material', 'articles' or 'supplies.' And additional compensation is provided to offset only Federal taxes of the type of sales taxes and processing taxes, 'applicable directly upon production, manufacture, or sale' and actually paid on supplies delivered to the Government. Since a tax on payrolls, or on the relationship of employment, is not—but in fact is distinct from—the type of tax 'on' articles represented by sales taxes and processing taxes, respondent is not entitled to the additional compensation which it seeks."

Respondent's contract specifically includes the processing taxes which were paid upon the materials used in the manufacture of the mechanics suits sold to the United States, hence the position of the respondent is supported by the decision of this Court in the Martin Company case.

Conclusion.

The decision of the Court of Claims is correct and there is no conflict of decisions. It is respectfully submitted, therefore, that the petition for certiorari be denied.

PHIL D. MORELOCK,
Attorney for Respondent.

August, 1940.

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Supreme Court of the United States

OCTOBER TERM, 1940.

No. 188.

THE UNITED STATES, PETITIONER,

VS.

COWDEN MANUFACTURING COMPANY,
RESPONDENT.

ON WRIT OF CERTIORARI TO THE COURT OF CLAIMS.

BRIEF FOR THE RESPONDENT.

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OPINION BELOW.

The opinion of the Court of Claims (R. 5) is reported in 33 F. Supp. 141.

JURISDICTION.

The judgment of the Court of Claims was entered April 1, 1940 (R. 11). The petition for writ of certiorari was filed June 27, 1940 (R. 12), and was granted October 14, 1940. Jurisdiction is conferred upon this court by Section 3(b) of the Act of February 13, ~~1935~~ 1925, as amended by the Act of May 22, 1939.

QUESTION PRESENTED.

Respondent on June 24, 1933, contracted to sell to the United States mechanics' suits at a certain price. The contract contained a clause providing for an addition to the purchase price of any federal taxes imposed after the date of the contract and "made applicable directly upon the production, manufacture or sale of the supplies covered by this contract and are paid by the contractor on the articles or supplies herein contracted for."

On August 1, 1933, processing taxes were imposed upon the materials used by the respondent in manufacturing the suits. These taxes were billed to the respondent by the processors as a separate item and under an agreement with the processors the respondent was compelled to pay the processing taxes. The processors in turn paid the processing taxes to the Collector of Internal Revenue.

Is the respondent entitled, under the provisions of its contract, to recover from the United States the processing taxes imposed subsequent to the date of the contract directly upon the manufacture of the materials used which respondent was compelled to pay to the processors?

STATEMENT.

Respondent is a Missouri corporation with offices at 412 West 8th Street, Kansas City, Missouri (R. 5).

On June 24, 1933, pursuant to a bid submitted on June 6, 1933, it entered into a contract, No. W-699-qm-4800 (O. I. 2538), with the United States through the proper purchasing officers of the Quartermaster Corps at Philadelphia, Pennsylvania, in which respondent agreed to sell to the United States and deliver at the Quartermaster Depot at Philadelphia, Pennsylvania, 23,496 suits, mechanics type B-1, at $1.90 for which the United States agreed to pay $44,642.40 (R. 6). In accordance with a change order dated July 5, 1933, under Article 7 of the contract, the total was increased upon written order from the proper contracting officer of the War Department and respondent was required to and did furnish 11,724 additional suits, mechanics type B-1 at $1.90 for which the United States agreed to pay $22,275.60 (R. 6). All suits, totalling 35,220, were delivered by the respondent, accepted and approved by the United States, and $66,918 paid by the United States to the respondent as provided by the contract (R. 6).

Both the bid made June 6, 1933, and the contract of June 24, 1933, contained the following provision:

> "Prices set forth herein include any Federal Tax heretofore imposed by the Congress which is applicable to the material purchased under this contract. If any sales tax, processing tax, adjustment charge or other taxes or charges are imposed or changed by the Congress after the date set for the opening of the bid upon which this contract is based, and made applicable directly upon the production, manufacture, or sale of the supplies covered by this contract and are paid by the contractor on the articles or supplies herein contracted for, then the prices named in this contract will be increased or decreased

accordingly and any amount due the contractor as a result of such change, will be charged to the Government and entered on vouchers (or invoices) as separate items" (R. 6).

Respondent, in the manufacture of the suits, used 213,127 3/4 yards of cotton cloth purchased from McCampbell and Company, 320 Broadway, New York, selling agents for the Graniteville Manufacturing Company of South Carolina, a first domestic processor. Also respondent used 885 2/5 units of cotton thread purchased from the American Thread Company. The confirmation of respondent's orders for said cotton cloth by McCampbell and Company contained the following provision (R. 6-7):

> "The prices stated herein are based upon present manufacturing conditions and cost thereunder. If such cost is increased by any federal taxes or by the administration of the Industrial Recovery Act, the Agricultural Adjustment Act or by any federal regulations or federally approved codes and practices, affecting costs, not now in force, the amount of such increased cost shall be added to the prices stated and delivery shall be extended in proportion to any limitation of production caused thereby."

The confirmation by the American Thread Company for respondent's order for cotton thread dated June 24, 1933, contained the following provision (R. 7):

> "In addition to the prices upon which this contract of sale is based, buyer agrees to pay any additional costs resulting from any sales tax or taxes and/or domestic allotment charges that may be imposed by the federal, state and/or local government and applicable to any items on this contract at time of shipment.'

Pursuant to the provisions in the confirmations, McCampbell and Company billed the respondent as a separate item for processing tax in the amount of $4,425.54 and the American Thread Company billed the respondent as a separate item for processing taxes in the amount of

$44.44. These taxes were paid by the respondent to the processors and in turn by them paid to the Collector of Internal Revenue (R. 7).

Respondent duly made claim and demand against the United States with the War Department for an increase in its contract price of $4,469.98 which was the processing tax imposed upon the processing of the cotton used in the manufacture of the cloth purchased and used by the respondent in the manufacture of the mechanics' suits furnished by the respondent to the United States (R. 7-8).

Thereafter, the claim was referred to the Comptroller General of the United States and was denied and rejected by the Comptroller General in his decision dated August 11, 1936, A-68085 (R. 8).

The Secretary of Agriculture, pursuant to the authority vested in him by the provisions of the Agricultural Adjustment Act of May 12, 1933 (48 Stat. 31), as amended, prescribed that the first marketing year for cotton began August 1, 1933. The tax was fixed at 4.2 cents per pound beginning August 1, 1933. The processing taxes of $4,469.98 were assessed and paid subsequent to the date of the contracts entered into between the respondent and the War Department and subsequent to the agreements between the respondent and the processors (R. 8).

This suit was filed December 1, 1938, in the Court of Claims of the United States (R. 1), which rendered an opinion in favor of (R. 5) and entered judgment for the respondent in the amount of $4,469.98 on April 1, 1940 (R. 11).

SUMMARY OF ARGUMENT.

The controversy herein arose and developed as the consequence of the Government refusing to reimburse the respondent under the provisions of a contract for processing taxes on materials used by the respondent in supplies furnished under the contract, paid by the respondent to the processors.

The question does not involve the claim of a taxpayer for the recovery of a tax erroneously and illegally collected. The right of the respondent to recover depends upon the provisions of its contract with the Government.

The processing taxes paid by the respondent to its vendors were "applicable directly" upon the manufacture of the supplies and falls squarely within the provisions of the contract. Any other interpretation would produce unreasonable and unwarranted results.

The authorities cited by the Government as supporting its position have no direct bearing upon the interpretation of respondent's contract with the Government, but if there is an inference to be drawn from these decisions it is favorable to the respondent.

The Court of Claims has decided the identical issue here involved in favor of the plaintiffs in four cases and in so far as we know there is no conflict.

ARGUMENT.

I.

The origin and development of the controversy.

The Agricultural Adjustment Act (48 Stat. 31) was approved May 12, 1933.

In enacting this legislation it was the purpose of Congress as set forth in Section 2(1) of the Act:

> "To establish and maintain such balance between the production and consumption of agricultural commodities, and such marketing conditions therefor, as will re-establish prices to farmers at a level that will give agricultural commodities a purchasing power with respect to articles that farmers buy equivalent to the purchasing power of agricultural commodities in the base period."

In order to carry out the purpose as indicated the Secretary of Agriculture was given the authority by Section 8 of the Act to provide among other things for the reduction of acreage employed in the production of any basic agricultural commodity and

> "to provide for rental or benefit payments in connection therewith * * * in such amounts as the Secretary deems fair and reasonable."

Section 9(a) of the Act provided:

> "When the Secretary of Agriculture determines that rental or benefit payments are to be made with respect to any basic agricultural commodity, he shall proclaim such determination and a processing tax shall be in effect with respect to such commodity from the beginning of the marketing year therefor next following the date of such proclamation. * * * The rate of tax shall conform to the requirements of Subsection (b)."

In Subsection (b) it is provided:

> "The processing tax shall be at such rate as equals the difference between the current average farm price for the commodity and the fair exchange value of the commodity; * * *."

However, if the Secretary of Agriculture concluded that the tax at such rate resulted in the accumulation of surplus stocks or a depression of the price of the commodity, then, and in that event, it is provided:

> "the processing tax shall be at such rate as will prevent such accumulation of surplus stocks and depression of the farm price of the commodity."

It was generally known in the spring of 1933 both before and after the enactment by Congress of the foregoing legislation that any concern which contracted with the Government to furnish materials and supplies processed from basic commodities would have to take into consideration the material effect of certain then unknown levies of taxes. In order that the Government might continue to purchase its supplies and the business concern might continue to sell these supplies to the Government where they were manufactured by the processing of basic commodities it was necessary to eliminate the uncertain factor of the tax until it was definitely determined and because effective with respect to the individual bids and contracts. In recognition of this situation the various purchasing agencies of the Government devised and incorporated in the bid and contract forms the "tax clause" of which the wording used in the bid and contract between the Government and the respondent in the instant case is typical providing as follows:

> "Prices set forth herein include any federal tax, heretofore imposed by the Congress which is applicable to the material purchased under this contract. If any sales tax, processing tax, adjustment charge, or other taxes or charges are imposed or changed by the Congress after the date set for the opening the bid upon which this contract is based and made applicable

directly upon the production, manufacture, or sale of the supplies covered by this contract and are paid by the contractor on the articles or supplies herein contracted for, then the prices named in this contract will be increased or decreased accordingly and any amount due the contractor as a result of such change will be charged to the Government and entered on vouchers (or invoices) as separate items."

The respondent submitted its bid on June 6, 1933, and the contract was awarded June 24, 1933. The above clause was contained in both the bid and contract (R. 6). In executing the contract both parties no doubt understood that no tax had at the date of the contract been imposed upon the materials to be used but on the other hand the parties were aware that such a tax might be imposed upon the materials to be used and it was the mutual agreement that in the event the contractor was forced to increase its costs by such tax then the contract price would be accordingly increased. The Secretary of Agriculture exercised the authority conferred upon him by Congress on July 14, 1933 (R. 11), and thereby fixed the rate of the tax and designated August 1, 1933, as the beginning of the marketing year with respect to cotton.

That the Government never intended that the tax be added to the bid and/or contract price by the respondent at the time same were consummated is amply illustrated by the correspondence between the parties in the case of *The Telescope Folding Furniture Company, Inc.*, v. *The United States*, 31 F. Supp. 780, 90 Ct. Cls. 635. There the bids for the supplies were submitted July 28, 1933, which was subsequent to the proclamation of the Secretary of Agriculture July 14, 1933, and prior to the effective date, August 1, 1933. Upon inquiry by the contractor as to whether or not the tax should be included in the bid the policy of the Government was clearly stated as follows:

"(a) If a federal processing tax is in *effect* at the time bids are opened, it will be presumed that

the successful bidder included the tax in his bid and no amount in excess of that bid will be paid by the Government.

"(b) If a federal processing tax becomes *effective* after bids are opened or after the contract is made, which tax must be paid by the vendor, the bid price may be increased accordingly in the manner stated in the 'Federal Taxes' paragraph in the invitations to bid, first above referred to.".

The respondent purchased the cotton cloth use in the manufacture of the supplies from McCampbell and Company, agents for the Graniteville Manufacturing Company, the first domestic processor and the cotton thread used from the American Thread Company, a first domestic processor. The respondent agreed to pay to its vendors any processing taxes which might be imposed upon the processing of the materials. The materials were furnished to the respondent and the invoices listed in addition to the agreed price for the materials and as a separate item processing taxes of $4,469.98 which were duly paid to the processors by the respondent. In turn the processors paid these taxes to the Collector of Internal Revenue.

Thus in accordance with the express provisions of the contract and the mutual understanding of the parties, respondent is entitled to recover from the Government the processing taxes paid on the materials.

II.

The respondent is not seeking as a taxpayer to recover taxes erroneously and illegally assessed and collected, but seeks to recover under a contract the taxes which it in turn was compelled under contract to pay to its vendors, thus increasing the cost of materials used in the furnishing of supplies provided under its contract with the Government.

The first case involving construction of the "tax clause" under analogous circumstances was that of the

Batavia Mills, Inc., v. *United States*, 85 Ct. Cls. 447. There the plaintiff purchased cotton shirting from the processor and paid to the processor the processing taxes. The Court of Claims rendered judgment in favor of the plaintiff for the amount of processing taxes paid by it to the processors. It was the contention of the Government that the plaintiff should not be permitted to recover because it did not actually pay the processing taxes to the Government. The court in rendering judgment for plaintiff said:

> "The ruling made by the Comptroller General cannot be sustained. This is not a suit for the refund of taxes paid but an action based upon the provisions of a contract. The provisions of law with reference to refunds of taxes collected under the Agricultural Adjustment Act have therefore no application. All the matters necessary to establish plaintiff's claim under the contract are shown. After the contract was entered into a new and additional tax was imposed on the manufacturer from whom the contract supplies were purchased by plaintiff. The tax was passed on by the manufacturer and under the terms of plaintiff's contract with the manufacturer it was obliged to pay it. Defendant expressly agreed that the amount of the tax should be added to the purchase price. The right of the plaintiff to recover the amount so paid is clear and judgment will be rendered accordingly."

In the case of *Righter* v. *United States*, 85 Ct. Cls. 699, the court rendered judgment in favor of the plaintiff on the same basis although in that case the plaintiff paid the processing taxes to his vendor which in turn paid it to the manufacturer of the supplies which in turn paid it to the first domestic processor. In the instant case and that of The Telescope Folding Furniture Company, *supra*, it has not abandoned its contention that recovery should not be had because the plaintiff did not pay the processing taxes to the Government, other points have been stressed in support of its position by the Government.

The plaintiff did not and is not entitled to file a claim for the recovery of the taxes as such and would only

have such right as a first domestic processor. After the Agricultural Adjustment Act was declared unconstitutional by this court on January 6, 1936 (*United States* v. *Butler*, 297 U. S. 1), Congress enacted Title VII of the Revenue Act of 1936, wherein it was provided that processors could file a claim with the Collector of Internal Revenue for recovery of the taxes which had been held to be unconstitutional and upon a showing that they had absorbed the taxes could recover. This respondent has no right to file such a claim under the provisions of Title VII of the Revenue Act of 1936, not having been the first domestic processor. Neither have respondent's vendors a right to recover under the provisions of Title VII of the Revenue Act of 1936, because it definitely passed on the taxes. The Government is not only in the position of having refused to abide by the terms of the contract, but has been unjustly enriched by the retention in its possession of unconstitutional taxes which, although absorbed by respondent, are not available to it except under the express provisions of the contract.

Even though the Government defended the *Batavia Mills Case* and the *Righter Case, supra*, before the Court of Claims on the ground that the plaintiff did not pay the taxes to the Government, yet the realization seemed to be prevalent that plaintiff should recover because in its briefs in these cases the Government said:

> "On the other hand, in a situation where the burden of the tax is passed on to the contractor from the 'processor' as here, the spirit, if not the letter, of the contract may require the reimbursement to the contractor of any amount equivalent to the processing tax here involved. Of course, under this interpretation of the contract, the burden is on the contractor to establish, as has been done in this case, that—
>
> (1) The 'processor' paid the processing and/or floor stock tax imposed by the Agricultural Adjust-

ment Act on the cotton from which the supplies involved here were manufactured, and

(2) The contractor in turn bore the burden of said tax, by reason of the actual increased cost to it and the payment of that additional amount for the supplies which it had agreed to deliver to the defendant."

The conditions as prescribed by the Government prevail in the instant case in that the processor passed the taxes on to the respondent and respondent's costs were increased thereby and furthermore the processor paid the taxes to the Government. As heretofore indicated it is respondent's contention that it should be reimbursed on account of the specific provisions of the contract in as much as the taxes were imposed and became effective after the contract to furnish the supplies had been executed. The fact that the taxes were invoiced to the respondent as a separate item and were so collected from the respondent merely serves to identify the liability of the Government under the express provisions of its contract.

The Government in defending the instant case before the Court of Claims endeavored to distinguish it from the Batavia Mills and Righter cases on the grounds that the contracts in those cases had been negotiated prior to, while the contract in respondent's case had been entered into subsequent to, the enactment of the Agricultural Adjustment Act May 12, 1933. The Government took the position that since the Agricultural Adjustment Act had been approved prior to respondent's contract it was on notice that the taxes should have been included in the bid and hence whether or not the tax were included in the bid, as a matter of fact, nevertheless technically the respondent was not entitled to recover. As heretofore indicated the Court of Claims had previously disposed of this question in its opinion in The Telescope Folding Furniture Company case wherein it had been definitely set out in correspondence between the plaintiff and the

Government with respect to bids made on July 28, 1933, subsequent to the proclamation of the Secretary of Agriculture July 14, 1933, fixing the rate of the tax and designating the first marketing year as August 1, 1933, that the tax should not be included in the bid unless and until the tax became effective. The Court of Claims considered very carefully the contention of the Government and shows that it was unknown when respondent's contract was negotiated whether or not there would be a processing tax on cotton; it was unknown when such a tax would become effective; the rate of any possible tax could not be determined; any rate which might be fixed was not assured of application because the Secretary of Agriculture might change it prior to its effective date and even after the rate became effective it might be altered by the Secretary of Agriculture. A more unstable and uncertain state of affairs could not have been created and as indicated by the court neither the respondent nor its vendors could have determined the tax, if any, that it would be necessary to pay and consequently to include such tax in the bid price, even if it had not been the policy of the Government to require that any tax should be omitted from the bid. The Court of Claims concludes (R. 11):

> "Under such circumstances we cannot say that these taxes had been 'imposed' prior to the date of plaintiff's contract with the defendant within the meaning in which that word was used in the contract. Authority had been conferred by Congress for the imposition of the tax, but that authority had not been exercised until thereafter, to-wit, on July 14, 1933. The purpose of the federal taxes provision of the contract was to reimburse the contractor for its additional costs brought about by the defendant's act in levying additional taxes. The taxes were not in effect when the contract was made and it was impossible for the contractor to ascertain when they would go into effect or the amount of them when they did. Therefore, it could not figure what to include in its costs on account of them. We are, therefore, of opinion that the processing taxes paid by the plaintiff

were taxes 'imposed or changed by the Congress after the date set for the opening of the bid upon which this contract is based.' The action of Congress in imposing the tax was not complete until action by its delegate, the Secretary of Agriculture, and this was after the contract was made" (R. 11).

III.

The processing taxes paid by the respondent to its vendors were "applicable directly" upon the manufacture of the supplies and fall squarely within the provisions of the contract. Any other interpretation would produce unreasonable and unwarranted results.

The respondent purchased the cotton cloth used in making the mechanics' suits from the manufacturer or processors through its agent, McCampbell and Company, and purchased the cotton thread from the manufacturer or processor, The American Thread Company. These vendors in accordance with their agreement with the respondent invoiced the processing taxes of $4,469.98 to the respondent as a separate item and the same were paid by the respondent in addition to the cost of the materials. The Government now contends in its brief (pages 8 and 9) that:

> "In the instant case the taxes certainly were not imposed upon the mechanics' suits."

At the same time the Government admits that

> "They (the taxes) were imposed upon the processors of the raw materials that were purchased and employed by the contractor in producing its final product for sale to the Government."

It is difficult to see why the fact that the respondent cut the cloth into shapes and sewed it together using the thread, a mere change in form and not substance, would serve to alter the responsibility of the respondent to its vendors or the responsibility of the Government to the respondent under the express provisions of the contract.

This same contention was advanced by the Government before the Court of Claims in the case of The Telescope Folding Furniture Company, *supra*, and was carefully considered by the court. The plaintiff in that case furnished cots to the Government, in the assembling of which it had used supplies processed from cotton purchased from a number of cotton processors. The court said:

> "The defendant makes no point of the fact that the contract was executed after the processing taxes on cotton had become effective, in view of the terms of the notice to bidders issued by the contracting officer. It, however, defends upon the ground that no processing tax was levied on cots, and that the so-called 'Federal Taxes' provision of the contract applies only to the articles furnished thereunder and not to the component parts thereof.
>
> Whether or not the defendant may be technically correct in this position, it is manifest that the plaintiff and the defendant's representative understood that there was not to be included in its bid any amount on account of processing taxes on any of the material used in making the cots, but that such taxes would be added to the contract price under the 'Federal Taxes' clause of the contract."

The court then considers the surrounding circumstances and conditions prevailing when the bids and contract were made which, as has heretofore been shown, prevail generally in all of these cases and then concludes:

> "In equity and good conscience, therefore, the plaintiff should recover the amount of the processing taxes paid by it, and the contract must be so construed by us, unless to do so would do violence to its plain and unequivocal meaning. We think it is susceptible of this construction."

The court then analyzes the tax clause in the contract as relating to defendant's contention:

> "The first sentence of the 'Federal Taxes' provision states that the prices set forth in the contract

do not include any federal taxes 'applicable to the material purchased' thereunder. The next sentence provides that if certain taxes are thereafter levied by Congress and made applicable to 'the production, manufacture or sale *of the supplies* covered by this contract, and are paid by the contractor, *on the articles or supplies herein contracted for*' such taxes are to be paid the contractor by the defendant (italics supplied by the court). While strictly speaking the 'material purchased' and the 'articles or supplies' were the cots, they include the cot's framework, the canvass covering and strap, and all its component parts.

If the plaintiff had contracted to furnish unassembled the framework for the cots and the canvass coverings and the strap, there could be no doubt that it would be entitled to recover for the processing tax paid on the covering and strap. The fact that it tacked the canvass covering and the strap to the framework and furnished the cot as an assembled article, we think, makes no difference.

The contractor did not pay the tax on the cots, but it did pay it on a part of the cots, namely, the canvass and strap. The payment of the tax on a part of the article was a payment of tax on the article itself."

As stated by the Government in the concluding paragraph of its brief (page 10) to which we subscribe:

> "The preference in the construction of contracts for an interpretation avoiding unreasonable or impossible results is well established. See Williston, Contracts (Rev. Ed., 1936), 1786 ff."

At the time before, when the contract was consummated, and subsequently there was never contemplated a tax on mechanics' suits, as such, in so far as any record shows. The tax was imposed upon the materials contained in such suits processed from basic commodities so designated by the Secretary of Agriculture under authority conferred upon him by the Congress under the provisions of the Agricultural Adjustment Act. To assume

that the parties had in mind, when the contract was made, anything other than the processing tax on the materials used in furnishing the supplies seems to be without foundation and an "unreasonable interpretation" which would produce unwarranted results. Such an interpretation increases respondent's costs of materials by the amount of the processing tax paid to its vendors under contract, and, in turn, permits the United States to profit by failure to comply with the specific provisions of a contract which the facts and circumstances clearly show were mutually understood between the parties to mean that respondent should recover such additional costs.

The Government on pages 9 and 10 of its brief maintains that the use of the word "directly" and the general character of the tax provisions indicate that reimbursement was not contemplated by the parties. It is also urged that any other construction of the contract than that urged by the Government would introduce the question of shifting of taxes and that the parties might have contracted on a cost plus basis or included an "equitable adjustment" clause.

It appears clear that the parties in using the word "directly" had in mind the addition to respondent's cost of materials of the tax subsequently imposed. It is true that other methods of expression or other bases of contact might have been used, but they were not, and the simple direct wording of the contract entered into was in all regards sufficient. In the case of *Cramp & Sons Ship and Engine Building Co.* v. *United States*, 72 Ct. Cls. 146, the court decided that the capital stock tax paid by the plaintiff for the year in which it was constructing a vessel under a cost plus contract represented a part of the cost prior to the computation of the percentage of profit. It would appear that if at all in point the decision of the court in that case would strengthen the position of the respondent here.

It is respectfully submitted that there is no question of the "shifting of taxes" or the "tracing of taxes" involved here. The court below has found as a fact that respondent paid the taxes to the processors and in turn the processor paid the taxes to the collector (R. 7).

IV.

The authorities cited by the Government as supporting its position have no direct bearing upon the interpretation of respondent's contract with the Government, but if there is an inference to be drawn from these decisions it is favorable to the respondent.

The Oswald Jaeger Baking Company v. *Commissioner*, 108 F. 2d 375 (C. C. A. 7, cert. denied), 309 U. S. 683; *Fuhrman & Forster Co.* v. *Commissioner*, (C. C. A. 7) p. 9600 Commerce Clearing House Tax Service, 1940 (not yet reported); *Zinsmaster Baking Co.* v. *Commissioner*, 109 F. 2d 738 (C. C. A. 8); *New Consumers Bread Company* v. *Commissioner*, (C. C. A. 3) p. 9633 Commerce Clearing House Tax Service, 1940 (not yet reported), are all cases wherein the United States Circuit Courts of Appeal reviewed the decisions of the United States Processing Tax Board of Review created by the Revenue Act of 1936 for the purpose of reviewing claims for refund of processing and/or floor stock taxes filed by the taxpayers with the Collector of Internal Revenue under the provisions of Title VII of the Revenue Act of 1936, after such claims had been rejected by the Commissioner of Internal Revenue.

These cases would not have arisen except for the fact that the Agricultural Adjustment Act was declared unconstitutional and involved the question of whether or not the litigants were entitled to a refund of taxes under the provisions of Title VII of the Revenue Act of 1936. Respondent's suit to recover the processing taxes paid its vendors has no basis under Title VII of the Revenue Act of 1936. On the other hand, respondent's claim arises

under the specific provisions of the contract and was affected in no way on account of the unconstitutionality of the Agricultural Adjustment Act.

The Government also cites the cases of *Lash's Products Company* v. *United States*, 278 U. S. 175, and *United States* v. *Glenn L. Martin Company*, 308 U. S. 62, which the Court of Claims in rendering judgment for the plaintiff in the case of *The Telescope Folding Furniture Company* v. *United States*, *supra*, considered with respect to the identical point raised by the Government in the case at bar and concluded that these cases are not in point. The court said:

> "The Lash's Products Company case did not involve the proper construction of a contract, which is the question of whether social security taxes came sented in the Martin case. That case involved only the question of whether Social Security taxes came within the 'Federal Taxes' provision."

It is our contention that the decision of this court in the Glenn L. Martin case strengthens the position of the respondent here. The Martin company contracted with the War Department to furnish aircraft and aircraft materials. The provisions of the "Federal Taxes" clause were substantially identical with those in the case at bar. Subsequent to the date of the contract, the Social Security Act became effective and the State of Maryland enacted an unemployment compensation law. The Martin company paid the United States $794.03 federal social security taxes and to the State of Maryland $6,943.29 unemployment compensation taxes with respect to *pay rolls* of employees who were engaged in work on the contracts in 1936 and 1937. The Martin company sought to recover from the United States the social security taxes and the unemployment compensation taxes paid alleging that such recovery was proper under the contract. In denying the right of the Martin company to recover under its contract this court said:

"Thus, this contract was concerned with federal taxes 'on' the goods to be provided under it, whatever the occasion for the taxes. And a tax 'on' the relationship of employer-employee—characterized as a tax on pay rolls—is not of the type treated by the contract as a tax 'on' the goods or articles sold.

"The contract refers only to federal taxes, existing or future, on 'material,' 'articles' or 'supplies.' And additional compensation is provided to offset only federal taxes of the type of sales taxes and processing taxes, 'applicable directly upon production, manufacture, or sale' and actually paid on supplies delivered to the Government. Since a tax on pay rolls, or on the relationship of employment, is not—but in fact is distinct from—the type of tax 'on' articles represented by sales taxes and processing taxes, respondent is not entitled to the additional compensation which it seeks."

Respondent's contract specifically includes the processing taxes which were paid upon the processing of the *materials* which respondent cut and put together in the form of mechanics' suits.

The cases of *Liggett Myers Tobacco Co.* v. *United States*, 299 U. S. 383, and *Wheeler Lumber Co.* v. *United States*, 281 U. S. 572, cited in a footnote at page 9 of the Government's brief involve the validity of tobacco and transportation taxes under the circumstances stated and do not appear to be in point here.

Conclusion.

The decision of the Court of Claims is correct and should be affirmed.

Respectfully submitted,

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Of Counsel:

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1940.

No. 188.

THE UNITED STATES OF AMERICA, *Petitioner*,

v.

THE COWDEN MANUFACTURING COMPANY, *Respondent*.

PETITION FOR REHEARING.

PHIL D. MORELOCK,
Counsel for the Respondent.

Of Counsel:
MORELOCK AND LAMB,
Washington, D. C.

PRESS OF BYRON S. ADAMS, WASHINGTON, D. C.

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PETITION FOR REHEARING.

To the Chief Justice and the Associate Justices of the Supreme Court:

Comes now the above-named Respondent, Cowden Manufacturing Company, a Missouri Corporation, and presents this, its petition for a rehearing of the above entitled cause, and, in support thereof, respectfully shows:

I.

The Court has erred in failing to recognize that the contract between the respondent and the United States was made in anticipation by both parties of the imposition of processing taxes on the "production and manufacture" of the materials used in making the suits.

At the time the contract between the United States and the respondent was entered into it was known by both parties that a processing tax would be imposed upon the processing of the materials to be used in the making of the suits. The respondent was not a processor and it was

known that it would be compelled to obtain the goods to be used in making the suits from a processor. The processing tax was not determined until July 14, 1933, whereas the contract had been entered into June 14, 1933. The processing tax was not and could not have been included in the bid or the contract price. It was the recognition of these facts which prompted the parties to agree that in addition to the contract price, as a part of respondent's costs, which did not and could not have included the processing tax, the respondent would be entitled to reimbursement for whatever amount of processing tax, if any, it was forced to pay. The function of the respondent in the process of manufacturing the supplies was the cutting of the cotton cloth and sewing it together into the specified shapes or finished article. This was well known to the parties and could not have been the reason for including the tax clause in the contract. If it had not been the intention of the parties that the respondent be reimbursed for the processing tax imposed upon the processing of the cloth used in making the suits there could have been no reason for the incorporation of the provision in the contract.

Knowing that the contemplated tax was on the production of the basic materials which would go into the garments and not on the cutting and putting together the component parts, and knowing that no tax of the latter kind was then thought of or afterwards established, let us look further at the clause and see what the parties must have had in mind. If the language in the tax clause had been thought to have the meaning ascribed to it by the Court, there could have been no reason to put it in the contract. It was known when bids were asked and when the contract was signed that there would be no processing tax on the operations of this respondent in assembling these garments. The term "supplies" as used in the tax clause must therefore have been intended to apply to the materials entering into the completed garment. The materials were the only thing entering into the transaction which could at that time have been reasonably in contemplation as subject to a proc-

essing tax. In other words, if the clause means what the Court has held it to mean, the parties would not have put it in the contract because they knew there would never be a condition which would make it applicable. We must assume that they acted reasonably and undertook by this language to provide for a situation which they definitely then contemplated would arise, and not that they were providing for one which they either knew would not arise or had no reason to anticipate. The whole purpose of the clause was to protect the contractor against increased costs which it could not then determine but which both parties definitely expected. We respectfully submit that the Court's construction of the clause is entirely too narrow, wholly disregarding the conditions under which and the purpose for which the clause was inserted.

The case of *United States* v. *Glenn L. Martin Co.*, 308 U. S. 62, does not support the decision of the Court in this case. There the corporation sued for the recovery of taxes under the provisions of the Tucker Act, 24 Stat. 505; 28 U. S. C. Para. 41(20). The taxes sought to be recovered were social security taxes and unemployment compensation taxes on payrolls of employees. These taxes were clearly outside of the provisions of the contract since they were not imposed upon the production and manufacture of materials delivered to the Government. As stated by this Court, the social security and unemployment compensation taxes were "on the relationship of employment" and were "distinct from * * * the type of tax 'on' articles represented by sales taxes and processing taxes".

It is evident from the facts in the case of *The Telescope Furniture Co.* v. *United States*, 31 F. Supp. 784, that under the terms of a contract identical with that under consideration here, the parties fully understood that the taxes imposed upon the processing of the materials used in the supplies were not to be included in the bid and that reimbursement was to be made to the company furnishing the supplies although not the processor. The bid in that case was made on July 28, 1933. Since the Secretary of Agriculture

had on July 14, 1933, prior to the bids, fixed the amount of the processing tax and had designated August 1, 1933 as the effective date, the company wrote to the War Department and asked whether or not the processing tax, then known, should be included in the bid.

The Government in response to the inquiry clearly stated its policy as follows:

> "(a) If a federal processing tax is in *effect* at the time bids are opened, it will be presumed that the successful bidder included the tax in his bid and no amount in excess of that bid will be paid by the Government.
>
> "(b) If a federal processing tax becomes *effective* after bids are opened or after the contract is made, which tax must be paid by the vendor, the bid price may be increased accordingly in the manner stated in the 'Federal Taxes' paragraph in the invitation to bid, first above referred to."

In that case it was known, as here, that the contractor was not a processor and would be compelled to acquire the materials to be used in the assembling of the canvas cots from the processor. It was known by the parties as in the instant case that the processing tax would have to be paid to the processor, who in turn would pay it to the Government. The use of the term "successful bidder" in paragraph (a) and the term "vendor" in paragraph (b) is significant and emphasizes that the parties intended that the contractor be reimbursed for the addition to its costs of any processing tax paid regardless of to whom paid. Otherwise the War Department could have written *which tax must be paid by the successful bidder to the Government.*

The War Department and the respondent were aware of the likelihood of a processing tax to be imposed upon the processing of the cloth and thread to be used by the respondent in making the suits. They were not able to determine the amount nor the time when the processing tax would become effective. It might not have become effective until after the respondent had completed its contract or the re-

spondent might have been able to furnish the supplies from stocks of goods on hand upon which no tax was required. However, as will be observed from the "Special Findings of Fact," made by the court below (R. 5-6-7), the respondent was compelled to purchase the goods with which to perform its contract from the processor after the tax became effective and was compelled to pay the processing tax which was billed to it as a separate item and not as a part of the purchase price of the goods. Consequently the only fair interpretation of the understanding of the parties is that respondent is entitled to reimbursement for the processing taxes paid which constituted additional costs to it.

II.

The Court has erred in failing to recognize and to give effect to the fact that the contract between the respondent and the Government was made prior to its agreement with the processors.

The Court, in its opinion, refers to the fact that the respondent contracted with the processors to purchase the cloth and thread and that these processors were liable for processing tax on the processing of these articles. The Court then said:

> "At the time these contracts were made no taxes were in effect on the processing of cotton, but in anticipation of such taxes respondent and the subcontractors agreed that respondent would reimburse them for any taxes they were required to pay on the processing of goods sold to respondent, the taxes to be billed as a separate item. Thereafter, respondent received the goods covered by these contracts and compensated the subcontractors for the taxes they were later required to pay on the processing of the cotton."

It is respectfully pointed out that the Court appears to have failed to recognize that the contract between the Government and the respondent was made prior to the contracts between the respondent and the vendors or proces-

sors. It was but natural and right that the respondent pass on to the vendors or processors the same rights of reimbursement which respondent understood to exist under its contract with the Government. There was no profit to any of the parties involved, it being the intent that the respondent pay the tax to the processor, the processor pay the tax to the Government and the Government return it to the respondent. The clause in the contract was primarily for the purpose of stabilizing the bid price to the Government and the purchase price of the materials to the respondent. The Government inserted the clause in the contract in order that respondent might properly determine its costs so as to submit its firm bid to the Government.

The tax clause of the contract was not inserted for the purpose of permitting the recovery of a tax as such. The purpose was that if the unknown element, be it tax or otherwise, should enter into the contractor's *cost*, it should in turn be added to the contractor's bid price. The processing tax represented this additional cost.

It was then necessary that the respondent afford the same protection to the processors from whom it purchased the cloth and thread. The Court has not recognized the existence of any obligation on the part of the Government to reimburse the respondent. The Court said:

> "We are of the opinion that the 'federal taxes' clause does not obligate the United States to reimburse its contractor for taxes which the latter has borne merely as a matter of contract with its subcontractors. On the contrary, the fair import of the clause is that the United States must make reimbursement only for such taxes as the contractor has paid pursuant to an obligation imposed upon him by the statute which exacts the tax."

It is respectfully urged that the proper interpretation of the contract must recognize that the respondent's agreement with the Government for its protection in making its bid was prior to its agreement with the processors and conversely the agreement with the processors followed and was in consequence of its agreement with the Government.

III.

As stated by the Court, "The language of the clause is precise". Therefore it is error to add to the clause by implication language which is not expressly written therein.

The part of the contract which appears to form the basis for the conclusions of the Court may be stated as follows:

> "If any * * * processing tax * * * are imposed * * * and made applicable directly upon the production, manufacture or sale of the supplies covered by this contract and are paid by the contractor on the articles or supplies herein contracted for, * * *"

In considering certain words and phrases in the above, the Court says:

> "The language of the clause is precise. It provides only for reimbursement of those taxes which are 'made applicable directly upon the production, manufacture, or sale of the supplies covered by this contract'. The supplies 'covered by this contract' are the mechanics' suits, the completed articles furnished to the United States. Since the clause further provides in exact language that the tax must be 'directly' applicable, we cannot agree that a tax on cloth, thread and labels is a tax on the supplies 'covered by this contract'. Compare Telescope Furniture Co. v. United States, 31 F. Supp. 780, 784; United States v. Glenn L. Martin Co., 308 U. S. 62."

It is respectfully submitted that the construction placed upon the contract by the Court to the effect that it was intended to and did contemplate the finished article, mechanics' type suits, is not only too narrow but was not the understanding of the parties. The Agricultural Adjustment Act, 48 Stat. 31, making provisions for a processing tax, as, if, when, and in such an amount as was designated by the Secretary of Agriculture, had been enacted May 12, 1933. The National Industrial Recovery Act, 48 Stat. 195, had been enacted June 16, 1933. The parties to this contract and

business men in general, where similar contracts were involved, were concerned with the processing tax which was known to be in the offing, and the additional costs caused by the administration of the National Industrial Recovery Act. At the time of this contract and during the course of its fulfillment there was no other revenue measure pending which would have affected the adjustment contemplated by the contract. The respondent not being a processor, there would have been no reason for the clause to have been inserted in the contract if it had been intended that it apply only to the finished article. It is difficult to see or understand why a general provision such as the one under consideration as to "production and manufacture" would have been written into the contract had it only contemplated the mechanics' type suits after they had been cut and sewed together by the respondent to the exclusion of the material or the operation upon the material which had to enter into the finished article. Suppose the respondent had been a processor and had processed the cloth and thread that went into the suits: the tax of $4,469.98 would have been the same, and the Government would have obtained the tax just the same. Then, if we correctly interpret the decision of the Court, the respondent should have been reimbursed under the contract. In fact, the Comptroller General would have authorized such reimbursement under his interpretation, and the case would never have been in Court. However, the Government has in its possession respondent's money the same as it would have, had the respondent been a processor. When we recognize that business in general and manufacturing in particular are diversified so as to cover a vast field of operation, it is readily apparent that the general clause in the contract had to be constructed so as to apply to all phases of such diversified operations and to each component part of the finished article, and, particularly, to the processing of the materials.

This contract was written by the Government. It is not to be believed that it was doing a useless thing. But it is respectfully submitted that if the language is to be interpreted as the Court has done, then it was an idle gesture to write in the tax clause. There was never any situation to which it could apply. Since the Government wrote the whole contract, if there be ambiguity it must be interpreted most strongly against the Government. We are convinced, however, that it requires only a reasonable construction consistent with the purpose for which it was written to meet a then anticipated and probable tax.

Where as in this case the processing of the materials, which was a part of the operation of manufacture, was done by a party different from the contractor, it was merely necessary to extend to that party the same protection as the contractor believed it had under its contract with the Government.

The Court said:

> "Moreover, the clause stipulates for reimbursement of taxes 'paid by the contractor'. It is reasonable to conclude that this phrase also contemplates payment of taxes to the United States in consequence of an obligation imposed by statute upon respondent. For while in a sense, perhaps, respondent 'paid' these processing taxes, it is more accurate to say that they were 'paid' by the subcontractors who merely shifted their burden to respondent as a separate item of the contract price. The clause as a whole indicates that this was the sense to be attributed to the phrase quoted."

In order to justify the construction indicated by the Court, it appears to us that there must be added to the quoted "paid by the contractor" the words *directly to the Government*. Is it not rather reasonable to assume that those who framed the clause in question, did not intend to confine the protection to those who paid the money directly to the Collector of Internal Revenue, and in formulating the clause contemplated just such a situation as existed here where the processor was merely a conduit

through which the money representing taxes passed from the respondent to the Government?

It is axiomatic that things which equal the same things are equal to each other. The tax came to the Government from the respondent through the processor, therefore the Government came into possession of the tax just the same as if it had received the check of the respondent. It does not appear that those who are responsible for the clause in the contract were concerned so much with the form and method of collection of the tax as they were with the question of whether as a matter of fact the Government received the tax. This was the attitude taken by Government Counsel when they were before the Court of Claims in the case of the *Batavia Mills, Inc.* v. *United States,* 85 Ct. of Cls. 447, as we have pointed out in our brief filed with the Court, at page twelve.

In this connection, it is important to refer to the facts as found by the Court below showing exactly what happened (R. 7). Pursuant to the protective clause which respondent had granted to the processors from whom it had purchased the cloth and thread, the processors billed the respondent *as a separate item for the exact amount* of the tax which they were to pay to the Government. The respondent then paid the processing tax to the processors.

As an ultimate fact with respect to the disposition of the tax, the Court below found (R. 7):

> "Processing taxes *in the same amount* were paid by Grantville Manufacturing Company, the processor, *to the Collector of Internal Revenue,* which amount was included in larger amounts of processing taxes paid by said processor." (Italics ours)

In other words, there can be no doubt of the fact that the Government was paid the tax of $4,469.98. It is difficult to see how any complex question of the incidence of the tax could arise from this simple state of facts. The Court with respect to this phase of the matter said:

> "A contrary construction of the 'federal taxes' clause introduces difficulties not contemplated by the parties. It would force them to trace the taxes back to the one upon whom the obligation first rested, whether the subsequent transactions were simple or complex. For if it could be said in this case that the processing taxes were imposed on the supplies covered by the contract and were paid by the contractor, it would be immaterial how far the contractor were removed from the original processor if the former could show that the burden of the tax had been shifted as the processed articles had changed hands and perhaps form. We can find nothing which suggests that the parties intended to draft a clause that would operate in such fashion."

In expressing the above thought and concern, we believe the Court had in mind the ordinary case involving the incidence of a tax. For example, if the tax is imposed upon A, who as a part of his sales price shifts it to B, who as a part of his sales price shifts it to C, and C, then, as a part of his sales price shifts it to X, Y and Z (the public), it is difficult to ascertain as to whom in the course of the procedure bore the burden of the tax and in what amount. In this type of case the rules *with respect to tax refunds* have been established in the cases of *United States* v. *Jefferson Electric Manufacturing Co.*, 291 U. S. 386, and *Lash's Products Company* v. *United States*, 278 U. S. 175.

The question of tax shifting as the term is ordinarily used does not enter into the situation here. There was really no shifting of taxes. As heretofore indicated, as a matter of protection, and in order that respondent could make a firm bid, the contract was entered into between the Government and the respondent. Then in turn the respondent granted to its vendors the same contractual protection. The Government fixed the amount of the tax which it determined to collect from the processor, who in turn sent the bill for the same amount to the respondent. If the respondent had been selling the mechanics type suits to customers other than the government no doubt the taxes would have been added to the sales price of the articles and then the tax would have

been shifted to the public. However, there existed a contract between the Government and the respondent to the effect that if the respondent would make to the Government a firm bid not including in its costs the processing tax then the Government would reimburse the respondent on account of any funds which the Government *as a matter of fact* collected from the respondent as processing tax, even though the tax were collected through another. This the Government failed to do and therein lies what we earnestly urge is our just complaint.

It appears to be immaterial that the form of the article upon which the tax was imposed changed from cloth to suits. The tax which is the subject of controversy did not change and as a matter of fact was specifically identified. Furthermore, that which we consider to be the meat of the contract has been found as a fact, to wit, *the Government collected the tax and now has the tax in its possession.*

IV.

The decision of this Court in substance grants to the Government a rebate and in effect relieves the Government from payment of the contract price for the supplies as provided by the contract.

In accordance with its contract with the Government and the amendment thereto, the respondent was to and did furnish to the Government 35,220 suits mechanics type B-1. The contract price paid to respondent was $66,918.00, or $1.90 per suit. It can readily be seen that after the purchase of material and payment of labor costs there could have been very little, if any, profit in making this price article. The Government then imposed a tax upon the processing of the materials used in making the suits of $4,469.98. If the respondent had not possessed other funds, it would have had to pay $4,469.98 out of the $66,918.00. In any event the facts show that the tax of $4,469.98 was paid to the Government through the processor so that the net amount paid out by the Government was $66,918.00 less $4,469.98, or

$62,448.02. In other words, the Government in effect received a rebate of $4,469.98 and whereas the contract called for the purchase price of the supplies to be $66,918.00, as an actual fact the supplies cost the Government $62,448.02. On the other hand, respondent, while receiving $66,918.00, was compelled to repay to the Government through the processor, $4,469.98, and consequently instead of $66,918.00, retained $66,918.00 less $4,469.98, or $62,448.02. In other words the price per suit was as a matter of fact reduced from $1.90 to $1.77 per suit, or 6.8 per cent reduction on gross sales value. It is a well known fact that the percentage of profit on Government contracts, owing to the competitive system of bidding, is not very large, and may well have failed to absorb the reduction.

It is our contention that the clause in question was inserted in the contract so that the bid price of $66,918.00 would be stabilized and that this full amount, no more and no less, should represent the cost of the supplies. As a matter of fact the Government has done that which it did not intend should be done by others, in that it has profited by a rebate of $4,469.98. The Government has the tax in its possession. Can the Government be permitted to profit at the expense of the respondent through such construction of language which appears precise and definite?

V.

Had Respondent and its vendors not relied upon the fulfillment of their contracts the tax might have been recovered under specific statute which remedy is not now available.

The respondent met its obligations to its vendors immediately upon the rendering of the invoices for $4,469.98. Then the respondent in 1933 requested payment from the Government of the $4,469.98 under the provisions of its contract. The claim of the respondent was under consideration in various stages until the final rejection by the Comptroller General in his decision of August 11, 1936,

A-68085 (R. 8). The claim of respondent was made upon the basis of its contract long before the Agricultural Adjustment Act as amended was declared unconstitutional by this Court on January 6, 1936 in the case of *United States* v. *Butler*, 297 U. S. 1. The origin of respondent's claim lay in its contract and was effective regardless of the constitutional status of the Agricultural Adjustment Act as amended.

Had it not been for the contractual relationship between the Government and the respondent and the contractual obligation between the respondent and its vendors there might have been a recovery of the tax as such after the Agricultural Adjustment Act was declared unconstitutional and Title VII of the Revenue Act of 1936 (49 Stat. 1648, 1747) was enacted by Congress. That Act provided: (Title 7 U. S. C. A. No. 644) entitled "Conditions on allowance of refunds":

> "No refund shall be made or allowed, in pursuance of Court decisions or otherwise, of any amount paid by or collected from any claimant as tax under this Chapter, unless the claimant establishes to the satisfaction of the Commissioner in accordance with regulations prescribed by him, with the approval of the Secretary, or to the satisfaction of the trial court, or the Board of Review in cases provided for under section 648 of this title, as the case may be—
>
> "(b) That he has repaid unconditionally such amount to his vendee (1) who bore the burden thereof, (2) who has not been relieved thereof nor reimbursed therefor, nor shifted such burden, directly or indirectly, and (3) who is not entitled to receive any reimbursement therefor from any other source, or to be relieved of such burden in any manner whatsoever." June 22, 1936, 9:00 P. M., C 690 ¶ 902, 49 Stat. 1747.

The Special Findings of Fact of the Court of Claims (R. 7) establishes that the respondent bore the burden of the tax. If it had not been for the contract with the Government for reimbursement, the respondent could have established that it could not have been relieved of the tax. If

the respondent's contract with the Government was not effective so as to establish the right to reimbursement then the respondent, after the enactment of the above statute, might have obtained relief through its vendors, who in turn could have obtained the refund from the Government of the $4,469.98 if they had repaid it to the respondent. However, the respondent having met its obligation to its vendors under contract made after and in reliance upon its contract with the Government, could not in good faith have requested reimbursement from its vendors. The vendors were not in any way benefited by the payment of the $4,469.98 to them by the respondent because they (R. 7) were the mere conduits through which the money flowed to the Government. The right of the processors to any claim for refund, even if they had voluntarily repaid the funds to the respondent after the enactment of the Revenue Act of 1936 expired July 1, 1937, as provided by the Act which time was later extended to January 1, 1940 by amendment to the Social Security Act.

It is respectfully urged that the respondent, having the contract for reimbursement with the Government and based thereon having extended the same rights to its vendors was bound in good conscience to maintain its claim for reimbursement with the Government and not with the vendors or processors.

For the foregoing reasons, it is respectfully urged that this petition for a rehearing be granted, and that the judgment of the Court of Claims be, upon further consideration, affirmed.

Respectfully submitted,

PHIL D. MORELOCK,
Counsel for the Respondent.

Of Counsel:
MORELOCK AND LAMB.

I hereby certify that the foregoing petition is presented in good faith and not for delay.

PHIL D. MORELOCK,
Counsel for the Respondent.

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SUPREME COURT OF THE UNITED STATES.

No. 188.—October Term, 1940.

United States, Petitioner,
vs.
Cowden Manufacturing Co., Respondent.

On Writ of Certiorari to the United States Court of Claims.

[January 13, 1941.]

Mr. Justice Murphy delivered the opinion of the Court.

Respondent seeks reimbursement from the United States of the amounts paid to processors to compensate them for processing taxes paid on cotton goods sold to respondent. The suit is based on a contract between respondent and the United States rather than on Title VII of the Revenue Act of 1936 (49 Stat. 1648, 1747) which authorizes refunds to processors, under certain circumstances, of processing taxes illegally collected under the Agricultural Adjustment Act (48 Stat. 31). The question is whether the "federal taxes" clause of the contract obligates the United States to make the reimbursement.

Prior to June 6, 1933, the War Department called for bids on a contract to furnish a certain kind of mechanic's suit. On June 6, 1933, respondent submitted its bid, and on June 24, 1933, executed a contract with the United States whereby respondent agreed to furnish a specified number of the suits at a stated price. The contract provided, in the "federal taxes" clause, that: "Prices set forth herein include any Federal Tax heretofore imposed by the Congress which is applicable to the material purchased under this contract. If any sales tax, processing tax, adjustment charge, or other taxes or charges are imposed or changed by the Congress after the date set for the opening of the bid upon which this contract is based and made applicable directly upon the production, manufacture, or sale of the supplies covered by this contract and are paid by the contractor on the articles or supplies herein contracted for, then the prices named in this contract will be increased or decreased accordingly. . . ."

To perform its contract with the United States, respondent contracted to purchase cotton cloth, thread, and labels from subcontractors who were liable, as processors, to pay any processing taxes levied on the articles sold to respondent. At the time these contracts were made no taxes were in effect on the processing of cotton, but in anticipation of such taxes respondent and the subcontractors agreed that respondent would reimburse them for any taxes they were required to pay on the processing of goods sold to respondent, the taxes to be billed as a separate item. Thereafter, respondent received the goods covered by these contracts and compensated the subcontractors for the taxes they were later required to pay on the processing of the cotton. It has performed its contract with the United States and now claims that the quoted provision obligates the United States to pay respondent the amounts it has paid its subcontractors to compensate them for the processing taxes they have paid. Because the Comptroller General rejected its claim, respondent brought this suit in the Court of Claims and obtained judgment. 32 F. Supp. 141. We granted certiorari on October 14, 1940, to resolve the uncertainty as to the correct construction of the "federal taxes" clause which appears in a large number of government contracts.

The only question is whether the United States, in the "federal taxes" clause, has agreed to pay respondent the amount respondent paid its subcontractors to reimburse them for taxes paid on the processing of the goods sold to respondent. We hold that it has not.

We are of opinion that the "federal taxes" clause does not obligate the United States to reimburse its contractor for taxes which the latter has borne merely as a matter of contract with its subcontractors. On the contrary, the fair import of the clause is that the United States must make reimbursement only for such taxes as the contractor has paid pursuant to an obligation imposed upon him by the statute which exacts the tax.

The language of the clause is precise. It provides only for reimbursement of those taxes which are "made applicable directly upon the production, manufacture, or sale of the supplies covered by this contract". The supplies "covered by this contract" are the mechanics' suits, the completed articles furnished to the United States. Since the clause further provides in exact language that the tax must be "directly" applicable, we cannot agree that a tax on the

cloth, thread, and labels is a tax on the "supplies covered by this contract". Compare *Telescope Folding Furniture Co.* v. *United States,* 31 F. Supp. 780, 784; *United States* v. *Glenn L. Martin Co.,* 308 U. S. 62.

Moreover, the clause stipulates for reimbursement of taxes "paid by the contractor". It is reasonable to conclude that this phrase also contemplates payment of taxes to the United States in consequence of an obligation imposed by statute upon respondent. For while in a sense, perhaps, respondent "paid" these processing taxes, it is more accurate to say that they were "paid" by the subcontractors who merely shifted their burden to respondent as a separate item of the contract price. The clause as a whole indicates that this was the sense to be attributed to the phrase quoted.

A contrary construction of the "federal taxes" clause introduces difficulties not contemplated by the parties. It would force them to trace the taxes back to the one upon whom the obligation first rested, whether the subsequent transactions were simple or complex. For if it could be said in this case that the processing taxes were imposed on the supplies covered by the contract and were paid by the contractor, it would be immaterial how far the contractor were removed from the original processor if the former could show that the burden of the tax had been shifted as the processed articles had changed hands and perhaps form. We can find nothing which suggests that the parties intended to draft a clause that would operate in such fashion.

We conclude that the quoted clause does not obligate the United States to compensate respondent for taxes which were paid by its subcontractors and were merely shifted to respondent pursuant to their subcontract. The judgment of the Court of Claims is reversed and the cause is remanded with directions to dismiss the petition.

It is so ordered.

A true copy.

Test:

Clerk, Supreme Court, U. S.